Supreme Court, U.S.
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No. OFFICE OF THE CLERK

In the
Supreme Court of the United States

MOHAMED POONJA, TRUSTEE,
Petitioner,

v.

JACK TRAMIEL,
Respondent.

On Petition for Writ of Certiorari to the United States Court of Appeals for the Ninth Circuit

PETITION FOR WRIT OF CERTIORARI

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QUESTIONS PRESENTED

1. 11 U.S.C. § 550 specifies that initial transferees may assert only those defenses "*otherwise provided*" in the section. The courts of appeals have held that § 550(a)(1) makes initial transferees *strictly liable* for the return of property or its value. The question presented is:

> Whether bankruptcy courts may invoke their equitable powers so that initial transferees are no longer strictly liable and, instead, may be allowed to assert defenses not *otherwise provided* in § 550.

2. This Court twice has established that "value" means *fair market value* when the property being valued is not (and was not) subject to proper foreclosure. The courts of appeals have applied this definition of "value" to 11 U.S.C. § 550(a). The question presented is:

> Whether bankruptcy courts may now construe "value," in § 550, to mean the *reasonably equivalent value*, rather than the *fair market value*, of property that was not subject to proper foreclosure.

3. 11 U.S.C. § 550(d) is a single satisfaction statute that allows non-settling defendants to receive settlement credits. This Court and the courts of appeals have held that only federal procedure controls whether to award settlement credits to reduce liability for 11 U.S.C. § 550 and similar federal claims. The question presented is:

Whether § 550(d) is no longer exclusively controlled by federal procedure so that settlement credits that would not be awarded under federal procedure may be awarded under state procedure.

PARTIES TO THE PROCEEDINGS

Petitioner is Mohamed Poonja. On August 20, 2010, Petitioner became the successor trustee to Suzanne Decker, who was the prior trustee of Debtor JTS Corporation's bankruptcy estate. Trustee was the plaintiff in the bankruptcy court, the appellant in the district court, and the appellee/cross-appellant in the Court of Appeals below. Petitioner will continue to refer to Ms. Decker as "Trustee."

Respondent is Jack Tramiel, who was a JTS director. Respondent was one of several defendants in the bankruptcy court. He was also the lone appellee in the district court and the appellant/cross-appellee in the Court of Appeals below.

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PETITION FOR A WRIT OF CERTIORARI

The Petitioner respectfully petitions this Court to grant a writ of certiorari to review the judgment of the United States Court of Appeals for the Ninth Circuit.

OPINIONS BELOW

The Court of Appeals' opinion is reported at 617 F.3d 1102 (9th Cir. 2010). App. 1a-33a. The Order Denying Cross-Motions for Reconsideration of the United States District Court, Northern District of California is reported at 2007 WL 1319531. App. 34a-40a. The district court's Order re Trustee's Appeal is reported at 2006 WL 284458781. App. 41a-59a. The Amended Judgment of the United States Bankruptcy Court, Northern District of California is unreported. App. 60a-63a. The bankruptcy court's Opinion Following Trial is unreported. App. 64a-117a. The bankruptcy court's Order Approving Good Faith Settlement is unreported. App. 118a-135a. The transcript of the bankruptcy court's December 22, 2005, hearing of the Motion to Amend Judgment is unreported. App. 136a-150a.

JURISDICTION

The Court of Appeals below entered its judgment on August 10, 2010. It denied Petitioner's petition for rehearing on October 14, 2010. App. 151a-152a . This Court has jurisdiction pursuant to 28 U.S.C. § 1254(1).

CONSTITUTIONAL AND STATUTORY PROVISIONS INVOLVED

The following Constitutional and statutory provisions are reprinted in the Appendix. App. 153a-174a.

U.S. Constitution Article I, Section 8, Clause 4
11 U.S.C. § 544
11 U.S.C. § 548
11 U.S.C. § 550
California Civil Code § 3439.07
California Civil Code § 3439.08
Indiana Code § 33-18-2-18
N.H. Rev. Stat. Ann. § 545-A:8
Uniform Fraudulent Transfer Act § 7
Uniform Fraudulent Transfer Act § 8
Fla. Stat. § 723.109

STATEMENT OF THE CASE

1. Statute At Issue

This case involves three distinct portions of a single section of the United States Code, Title 11 ("Code") – 11 U.S.C. § 550.[1] First, after stating in its opening clause that it makes transferees liable "except *as [it has] otherwise provided,*" § 550 provides the several specific defenses that transferees can assert to limit their liability. None of § 550's specified defenses is the defense that Respondent asserts.

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[1] All further references to "§" will be to sections of the Code, unless stated otherwise.

Second, after a bankruptcy trustee avoids a transfer under one of the Code's avoidance provisions, § 550 allows the trustee to recover the transferred property or its "value" from the transferees. § 550 does not define "value."

Finally, § 550(d) determines whether transferees are entitled to receive settlement credits that would reduce their liability. It fails to expressly state whether it is controlled by federal or state procedure.

Each of § 550's above portions is subject to intercircuit conflict.

2. Facts

JTS was insolvent at all relevant times. App. 83a. Because of its dire need for cash, JTS sought to sell eight unencumbered parcels of real property ("Parcels") to Respondent. App. 4a-5a, 69a. Respondent was a JTS director at the time. App. 4a, 67a, 69a.

The Parcels' fair market value was $15,760,000. App. 6a, 11a, 85a. Respondent had been the board chairman of the Parcels' previous owner, App. 4a, 67a, 69a, and knew that the Parcels were worth at least $12,000,000 to $13,000,000. App. 24a, 71a. Yet, when he learned that JTS wanted to sell the Parcels because of its dire financial condition, Respondent offered, on a "take it or leave it" basis, to purchase them for only $10,432,815 – *i.e.*, $10,000,000 in cash plus a one-year repurchase option ("Option") that the bankruptcy court valued at $432,815. App. 4a-5a, 69a, 83a, 88a-89a, 93a. Moreover, despite his being a JTS fiduciary, Respondent guaranteed himself a seven figure return

on the transaction by conditioning his offer on JTS's agreeing that if it exercised the Option, it would allow Respondent to keep the greater of $1,000,000 or the Parcels' rents collected during the option period ("Rents"). App. 4a-5a, 69a, 73a. The Rents ultimately totaled $1,387,185. App. 7a, 73a.

Although the Parcels were unencumbered and not subject to foreclosure, JTS agreed to Respondent's condition, and sold the Parcels while believing both that the price was fair "in light of [its] immediate need for funds," but likely less than fair market value. App. 5a. Still struggling financially, App. 5a, JTS never exercised the Option. App. 73a.

The Transfer's net effect was that Respondent paid $10,432,815 to JTS for the Parcels and Rents (together "Properties"), which had an aggregate value of $17,147,185 (*i.e.*, Parcels' $15,760,000 fair market value plus Rents totaling $1,387,185). Respondent no longer owns the Parcels. He transferred them into an entity for his children. App. 73a.

3. Bankruptcy Court

Pursuant to 28 U.S.C. § 157 and § 1334, Trustee filed a complaint with the United States Bankruptcy Court, Northern District of California asserting multiple claims for relief for various unrelated injuries that JTS had suffered. These claims included a claim to avoid the Transfer as a constructive fraudulent transfer under § 544(b) and a related claim under § 550 to recover the Properties' value from

Respondent.[2] App. 65a-66a. Only Respondent was asserted by Trustee to be liable for the Transfer as a transferee. Respondent's co-defendants were asserted to be liable for the Transfer only as directors, conspirators, and aiders and abetters, but not as transferees.

Prior to trial, the bankruptcy court entered an order approving a $4,500,000 settlement between Trustee and Respondent's co-defendants. App. 119a-135a. The settlement order recognized that federal procedure controlled whether Respondent would receive a settlement credit by stating that the court would consider granting a settlement credit request only if two necessary federal criteria were met – *i.e.*, (1) the court's finding that the settling co-defendants were jointly liable; and (2) the court's allocation of proportional culpability among all jointly liable defendants. App. 122a. The court's subsequent joint pre-trial order did not designate as trial issues whether the settling co-defendants were jointly liable as conspirators or what their relative culpability was.

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[2] In bankruptcy actions to recover fraudulent transfers, profits, rents, and proceeds generated by the recovered property are also recoverable. *See Rudin v. Steinbugler*, 103 F.2d 323, 326 (2nd Cir. 1939) (transferee of fraudulent transfer was liable both for fraudulently transferred property and any derivative profit because such profits equitably belong to the creditors); *In re Schwartz*, 383 B.R. 119, 127 (B.A.P. 8th Cir. 2008) (an avoided mortgage's Section 550 value includes mortgage payments made to the transferee); *In re Burke*, 60 B.R. 665, 669 (Bankr. D. Conn. 1986) (the right to rent is part of real property transferred, so "it would be incongruous for the transferee to be able to keep the rental or sale proceeds" of property that is recoverable by the estate). Trustee, however, limited her recovery request to only those rents collected prior to the Option's October 1996 expiration.

Nor did the court amend its pre-trial order to add those issues. Further, neither Trustee nor Respondent raised those issues at trial.

After trial, the bankruptcy court calculated the Parcels' reasonably equivalent value to determine whether the Transfer was a constructive fraudulent transfer pursuant to California's fraudulent transfer law.[3] Finding that the Parcels' fair market value was $15,760,000, App. 11a, 85a, the court calculated the Parcels' reasonably equivalent value. It opined that the Parcels' reasonably equivalent value was 75% of their fair market value – *i.e.* $11,820,000 – based on JTS's willingness to "take a reduced price" to "obtain funds quickly" because of its "dire need for cash." App. 6a, 11a-12a, 86a-88a. The court concluded that the Transfer was a constructive fraudulent transfer because the $10,432,815 paid by Respondent was less than $11,820,000. App. 6a, 89a-90a.

After finding that the Transfer was a fraudulent transfer, the bankruptcy court rejected Trustee's argument that § 550 allowed her to recover the Properties' entire *fair market value* of $17,147,185 from Respondent. Instead, the court construed § 550 to mean Respondent was liable for the Parcels' $11,820,000 *reasonably equivalent value*. App. 89a-90a. The court then rejected Trustee's argument that Respondent was not entitled to reduce his § 550 liability by the $10,432,815 that he had paid JTS. Instead, the court held that Respondent could reduce

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[3] California Civil Code § 3439.01 *et seq.* All further references to sections of the California Civil Code will be to " CC §", unless specifically stated otherwise.

his liability by that amount using CC § 3439.08(d)(3),[4] despite its not being "otherwise provided" as a defense in § 550. The court reasoned that CC § 3439.08(d)(3) would have been available to Respondent as a defense had a creditor brought a recovery action against him under UFTA § 7(a)(1).[5] App. 7a-8a. The court also rejected Respondent's request for a $4,500,000 settlement credit ("Credit"). App. 114a.

At a post-trial hearing on the parties' motions to amend the original judgment, the bankruptcy court made several additional findings. First, notwithstanding Trustee's argument to the contrary, the court found that Respondent's request for the Credit was a matter of state law and controlled by California procedure rather than by federal procedure. App. 143a-144a. Second, it found that Trustee's second amended complaint involved "multiple claims for multiple injuries arising from several independent business transactions." App. 145a. Third, it found that the co-defendants were tortfeasors because Trustee had alleged that they were liable for the Transfer, but it did not make its own finding that settling co-defendants were jointly liable or allocate culpability[6] Finally, the court awarded Trustee

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[4] For purposes of clarity and consistency, Petitioner hereafter will refer to CC § 3439.08 and all other sections of the state versions of the Uniform Fraudulent Transfer Act as ("UFTA §").

[5] CC § 3439.07(a)(1)

[6] The bankruptcy court stated:

> [T]he Trustee also alleged that the settling defendants were responsible for the estate's injuries arising out of the sale of the real property to Tramiel, and those claims were covered by

prejudgment interest of 7% per annum, App. 62a, and reversed itself by granting the Credit. App. 63a.

Based on the above, Respondent had no net liability for the Transfer because his $11,820,000 liability was less than the combined credits for his $10,432,815 payment and his co-defendants' $4,500,000 settlement payment.

4. District Court

Invoking 28 U.S.C. § 158(a), Trustee appealed to the district court, which partially affirmed and partially reversed the bankruptcy court. App. 59a. Partially reversing the bankruptcy court, the district court adopted Trustee's position that the term "value" in § 550 required an award of the Properties' $17,147,185 *fair market value*. App. 8a, 52a-53a. Partially affirming the bankruptcy court, it rejected Trustee's position that Respondent could not assert UFTA § 8(d)(3) to reduce his liability by $10,432,815 because the defense was not provided in § 550. App. 8a, 52a-53a. Finally, the district court reversed the bankruptcy court's award of the Credit by adopting Trustee's position that Respondent was not entitled to the Credit, in part, because joint liability was not found. App. 8a-9a, 56a. Ultimately, the district court found that Respondent's liability was $6,714,370 ($17,147,185 less $10,432,815). App. 8a-9a, 59a.

> the settlement at issue. Thus, with respect to the real property transaction, the settling defendants were tortfeasors claim (sic) to be liable for the same tort as Tramiel, the failure to pay reasonably equivalent value.

App. 145a.

5. Ninth Circuit Court of Appeals

Pursuant to 28 U.S.C. § 1291, Respondent and Trustee appealed and cross-appealed, respectively, the district court's order to the Ninth Circuit Court of Appeals. The Court of Appeals panel ("Panel") heard oral argument on November 6, 2009. It published its Decision on August 10, 2010, partially affirming and partially reversing the district court.

Consistent with both lower courts, the Panel concluded that the Transfer was a fraudulent transfer under California law and void under § 544(b). App. 23a. Regarding "value," the Panel concurred with the bankruptcy court's finding, based on the experts' testimony, that the Parcels' *fair market value* was $15,760,000 and that their *reasonably equivalent value* was $11,820,000. App. 11a-12a. It, however, reversed the district court, and found that "the fair market value ... was [not] determinative" of "value" for §550's purposes, thus construing "value" in § 550 to mean the Parcels' *reasonably equivalent value*. App. 11a-12a, 33a.

Regarding whether transferees are entitled to assert defenses not expressly provided in §550, the Panel found that they were entitled. It held that § 550's equitable and restorative purpose and Congressional intent enabled the bankruptcy court to invoke its equitable power to permit Respondent to assert UFTA § 8(d)(3) despite its not being provided in § 550. Relying *solely* on policy and intent and without any mention of § 550's text or consideration of its plain meaning, the Panel wrote:

> [T]he amount of recovery ... must further the *intent* of § 550 to promote equity and restore the estate to its prior condition.
>
> ***
>
> This conclusion effectuates the *intent* of § 550 to restore the bankrupt estate to the financial condition it enjoyed prior to the transfer. [citation omitted] Allowing the estate to profit by taking value that should be returned to a good faith transferee does not promote the *purpose* of § 550 to restore equity. [citation omitted] Moreover, allowing state law good faith transferee exceptions in cases asserting § 544 claims permits a *symmetry* with the Bankruptcy Code: § 548 of the Bankruptcy Code, which voids fraudulent transfers under federal law, allows for a reduction in recovery due to a good faith transferee. Section 544(b) ... should reflect this *symmetry*.

App. 23a, 25a (emphasis added).

Finally, the Panel reversed the district court by granting the Credit. The Panel based its award on California procedure, which the Panel held had been satisfied. App. 25a-33a. The Panel did not address Trustee's position that the Credit was subject to federal procedure, and that the settlement credit

criteria under federal procedure had not been satisfied.[7]

Trustee petitioned for a rehearing. But on October 14, 2010, Trustee's petition was denied.

REASONS FOR GRANTING THE PETITION

In addition to its obvious importance to the parties (who have tens of millions of dollars at stake) that the issues be correctly decided, the issues in this case are important because they involve intercircuit conflicts. And a heightened need to resolve these intercircuit conflicts exists because they involve issues of bankruptcy, which is constitutionally mandated to be uniform, and federal procedure, which also needs to be uniform. Furthermore, the impact of denying certiorari would go well beyond its impact on § 550 because the Panel's erroneous reasoning strikes at the very methodology of statutory construction for Code cases that this Court has established carefully over time. Because each of the intercircuit conflicts in this case is outcome-determinative, unless the intercircuit conflicts are resolved, they will result in unequal treatment of parties based on nothing more than venue, which is a recipe for increased forum shopping.

Moreover, the need for the granting of certiorari in this case is amplified by additional factors. Because the issues are not fact sensitive, this case presents this Court with an exceptional opportunity to resolve the

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[7] The Panel implied that, for purposes of awarding the Credit, it was sufficient that Trustee had alleged the settling co-defendants were liable. App. 29a-30a.

underlying conflicts completely and finally using broad rules. The laying down of broad rules will relieve an overburdened judicial system by increasing the predictability that guides: (1) lower courts when they construe the Code; (2) lawyers when they formulate strategy and advise their clients; and (3) parties when they decide whether to file or settle litigation or seek bankruptcy protection. Such relief is particularly helpful because the number of bankruptcy filings continues to explode and § 550 reaches into every bankruptcy case regardless of chapter.

I. THE CIRCUITS ARE IN CONFLICT OVER WHETHER INITIAL TRANSFEREES ARE STRICTLY LIABLE AND MAY ASSERT DEFENSES NOT PROVIDED IN § 550.

Instead of holding Respondent strictly liable for the Properties' full value, the Decision allows him to reduce his liability by asserting defenses not otherwise provided in § 550. It is in *direct conflict* with the decisions of this Court and the courts of appeals, which find that initial transferees are strictly liable and may not assert defenses that § 550 does not expressly provide. Because it is erroneous, the Decision allows Respondent to escape liability for more than $17,000,000 (the $10,432,815 of improperly reduced liability plus the 7% annual prejudgment interest awarded by the bankruptcy court). This amount should be made available for equitable distribution to all of JTS's creditors rather than retained by Respondent.

A. The Decisions Of The Courts Of Appeals Hold That Initial Transferees Are Strictly Liable And May Not Assert Defenses That Are Not Otherwise Provided In § 550.

Multiple decisions by the courts of appeals hold that initial transferees are "strictly liable" for the value of voidably transferred property – regardless of the transferees' good-faith. *See e.g., In re Red Dot Scenic, Inc.*, 351 F.3d 57, 58 (2nd Cir. 2003) ("bankruptcy code imposes *strict liability*" on initial transferees) (emphasis added); *In re Hurtado*, 342 F.3d 528, 532-33, 534 n.2 (6th Cir. 2003) ("*As is plain from its text*, section 550(a)(1) holds initial transferees *strictly liable* for any fraudulent transfers they receive") (emphasis added); *In re Cohen*, 300 F.3d 1097, 1107 (9th Cir. 2002) (holding initial transferees "*strictly liable*" is a Congressional policy choice) (emphasis added); *Rupp v. Markgraf*, 95 F.3d 936, 944 (10th Cir. 1996) (holding initial transferees "*strictly liable*" is fair and equitable in bankruptcy) (emphasis added); *cf. Bonded Fin. Servs., Inc. v. European Am. Bank*, 838 F.2d 890, 894 (7th Cir. 1988) (noting that it is "misleading" to analyze § 550 in a way that allows courts to "excuse the [initial] transferee from repaying using equitable powers").

Transferees may not escape their strict liability by asserting defenses not "otherwise provided" in § 550. Transferees who have attempted to do so have had their arguments rejected by the Seventh Circuit Court of Appeals and a different panel of the Ninth Circuit

Court of Appeals.[8] In fact, the Seventh Circuit case involved Indiana's UFTA § 8(d)(3),[9] which is the same as CC § 3439.08(d)(3), the state law defense that the Decision permits Respondent to assert.

In *Boyer v. Crown Stock Distribution, Inc.* (*Boyer-III*), 587 F.3d 787 (7th Cir. 2009), the court reviewed two lower court decisions that held a debtor's sale of assets to be a fraudulent transfer under Indiana law and therefore void under § 544(b). *Boyer v. Crown Stock Distribution, Inc.* (*Boyer-II*), 2009 WL 418275 (N.D. Ind. 2009); *In re Boyer* (*Boyer-I*), 2006 WL 6401548 (Bankr. N.D. Ind. 2006). In *Boyer-II*, the district court recognized that a bankruptcy estate's recovery of fraudulent transfers is "governed by § 550(a), irrespective of any recovery limitation imposed by [state] law." *Boyer II*, 2009 WL 418275 at *16. Consistent with this, the court rejected the immediate transferees' use of UFTA § 8(d)(3), which it recognized as a defense that § 550 does not provide. *Id.* at *15-16, 18; *see also Boyer-I*, 2006 WL 6401548 at *12, 14, 16.

The Seventh Circuit affirmed the lower courts.[10] It rejected the UFTA § 8(d)(3) argument without discussion by letting stand the immediate transferees' liabilities without reduction for the amount paid.

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[8] This Court considers intracircuit conflicts when intercircuit conflicts also exist. *See e.g., Inyo County, Cal. v. Paiute-Shoshone Indians of the Bishop*, 538 U.S. 701, 709 & n.5 (2003).

[9] Indiana Code § 32-18-2-18(d)(3).

[10] *Boyer-III* reversed one finding regarding a $590,328 dividend payment, but that payment is irrelevant to this discussion.

Boyer-III, 587 F.3d at 798. Because the UFTA § 8(d)(3) argument was considered in *Boyer-III*[11] and its resolution essential to the Seventh Circuit's affirmance, *Boyer-III* has precedential value, and qualifies as a basis for granting certiorari. *See Anderson v. Celebrezze*, 460 U.S. 780, 784 n.5 (1983) (precedential effect of affirmances extends to "the precise issues presented and necessarily decided"); *Id.* at 786 & n.6 (courts of appeals' summary affirmances create conflicts warranting certiorari).

Like the Seventh Circuit, the Ninth Circuit rejected the use of defenses that § 550 does not expressly provide. In *In re Straightline Investments, Inc.*, 525 F.3d 870 (9th Cir. 2008), the bankruptcy court avoided the debtor-in-possession's unauthorized postpetition transfer of $200,600 of accounts receivable. The estate successfully sued to avoid the transfer. It recovered the full value of the accounts while also keeping the $186,455 that the transferee had paid for those accounts. The Ninth Circuit discussed, and ultimately rejected, two factually distinguishable cases that allowed initial transferees to reduce their liability using equitable defenses that § 550 did not provide – *i.e.*, *In re Sawran*, 359 B.R. 348, 353 (Bankr. S.D. Fla. 2007), and *In re Cybridge Corp.*, 312 B.R. 262, 269-70 (D.N.J. 2004). Noting that equitable defenses are not expressly provided in § 550, the Ninth Circuit rejected the transferee's assertion of an equitable setoff defense to recover the money he had paid the estate. *Straightline*, 525 F.3d at 884-85. Consequently, the initial transferee remained strictly

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[11] Appellee/Cross-Appellant's Brief to the Seventh Circuit Court of Appeals, 2009 WL 1900130 at Section VII., Argument VIII.

liable for the transferred property's entire value, and received no reduction for the amount that he paid. *Id.*

Boyer-III and *Straightline* arrived at their holdings by applying the methodology that this Court has carefully developed over time to provide courts and parties with some degree of predictability in Code matters. This methodology requires that the plain meaning of Code sections must be applied unless the result would be absurd. *Lamie v. U.S. Trustee*, 540 U.S. 526, 534 (2004); *U.S. v. Ron Pair Enterprises, Inc.*, 489 U.S. 235, 242 (1989) (plain meaning is conclusive unless demonstrably contrary to drafters' intentions). History and underlying policy must be disregarded when a Code section has a plain meaning that is not absurd. *Union Bank v. Wolas*, 502 U.S. 151, 163 (1991) (Scalia, J. concurring). Furthermore, when interpreting a single Code provision, courts should note when language in that provision is either absent from or included in a different Code provision. *Milavetz, Gallop & Milavetz v. U.S.*, 130 S.Ct. 1324, 1332 (2010) (interpreting "debt relief agencies" by noting that "attorneys" is not among the listed statutory exceptions); *BFP v. Resolution Trust Corp.*, 511 U.S. 531, 536 (1994) (recognizing presumption that Congress acts intentionally when it includes particular language in one section of a statute but not another).

§ 550's opening clause states that trustees can recover property or its value "*[e]xcept as otherwise provided in this section.*" The clause's plain meaning is that transferees may assert only those defenses provided in § 550 to escape or reduce their liability. Noting that the transferees' defenses were not among those provided in § 550, *Boyer* and *Straightline* both

rejected the assertion of those defenses. It is the only correct conclusion a court applying this Court's methodology could reach.

B. The Decision Is Erroneous And Conflicts Directly With The Above Cases Because It Finds That Initial Transferees Are Not Strictly Liable And May Assert Defenses Not Otherwise Provided In § 550.

By holding an initial transferee was not strictly liable because he could assert a UFTA § 8 defense, which § 550 does not expressly provide, the Decision *directly conflicts* with almost all courts of appeals cases, including *Boyer-III* and *Straightline*. The Decision arrives at its peculiar holding due to the methodology it employed to construe § 550. This methodology was expressly rejected by this Court, which requires a different methodology. And it is unalterably incompatible with the methodology used by other courts of appeals.

The Decision eschews §550's plain meaning. Instead, it is based openly and solely on what the Panel perceived to be § 550's underlying intent and policy. App. 15a, 23a, 25a. Without any mention of § 550's text, the Decision states:

> [T]he amount of recovery ... *must further the intent* of § 550 *to promote equity* and restore the estate to its prior condition.
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> This conclusion *effectuates the intent* of §.550 to restore the bankrupt estate to the financial

> condition it enjoyed prior to the transfer. Allowing the estate to profit by taking value that should be returned to a good faith transferee does not *promote the purpose* of § 550 to restore equity. Moreover, allowing state law good faith transferee exceptions in cases asserting § 544 claims *permits a symmetry* with the Bankruptcy Code: § 548 of the Bankruptcy Code, which voids fraudulent transfers under federal law, allows for a reduction in recovery due to a good faith transferee. Section 544(b) ... *should reflect this symmetry*.

App. 23a, 25a. (emphasis added; citations omitted).

The Decision's result and methodology are supported by one other Court of Appeals case – *In re Kingsley*, 2007 WL 1491188 (Bankr. S.D.Fla. 2007), *aff'd* 518 F.3d 874 (11th Cir. 2008).[12] *Kingsley* allows the initial transferee to escape strict liability by asserting Florida's UFTA § 8(c).[13] It, too, ignores §550's plain meaning, relying, instead, solely on policy and equitable considerations. *See Kingsley*, 2007 WL 1491188, at *4-6; *Kingsley*, 518 F.3d at 877-78. The

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[12] *In re Jackson*, 459 F.3d 117 (1st Cir. 2006), does not support the decision. In *Jackson*, the First Circuit affirmed *In re Jackson*, 318 B.R. 5, 26-27 (Bankr. D.N.H. 2004), which ruled that an estate's recovery was subject to equitable defenses allowed under New Hampshire's UFTA § 8 (N.H. Rev. Stat. Ann. 545-A:8(III)). While the lower court case supported the Decision, the First Circuit's affirmance does not because the parties before the First Circuit never challenged the lower court's ruling regarding UFTA § 8. *Jackson*, 459 F.3d at 127. Thus, the issue of whether UFTA § 8 applies to § 550 was never before the First Circuit.

[13] Fla. Stat. § 726.109(2).

Decision and *Kingsley* compound their erroneous reliance on §550's underlying policies by both incorrectly analyzing those policies and incorrectly applying them.

For instance, the Decision states that bankruptcy's policy of doing equity requires initial transferees to recoup, through a reduction in their § 550 liability, the entire amount that they paid to the debtor. But that result does not do equity under the Code. The Code's main policy goal is "to secure equal distribution among creditors." *Howard Delivery Service, Inc. v. Zurich American Ins. Co.*, 547 U.S. 651, 655 (2006). And it achieves this goal in the context of successful recovery actions by providing transferees with a single remedy to recoup the amounts that they had paid to the debtor. The single remedy provided by the Code is the right to file an unsecured claim for the amount paid to the debtor, but only *after* the transferees return the property's full value. 11 U.S.C. § 502(d), (h); Fed.R.Bankr.P. 3002(c)(3). This remedy accomplishes equitable distribution by allowing all creditors to share *pro rata* in a distribution of the money paid by the transferee plus the full value of the property that the debtor transferred. Limiting Respondent to this remedy is not harsh because, in addition his receiving a $10,432,815 claim for the value he gave to JTS, he will not have to return the Parcels, which had a $15,700,000 fair market value in 1996, or any profit or income generated by the Parcels other than the Rents.

The Decision and *Kingsley* are the only Court of Appeals decisions that do not recognize that, in bankruptcy, equity actually *precludes* initial transferees from being made whole at the expense of a bankruptcy estate trying to recover the full value of

transferred property. *See e.g., Rupp,* 95 F.3d at 944 (it is equitable "to make the [initial transferee] bear the risk of the fraudulent nature of this transaction rather than [the] other creditors"); *Straightline*, 525 F.3d at 884-85 (§ 550 is "substantially less protective of transferees than it is of the estate"); *In re Skywalkers,* 49 F.3d 546, 549-50 (9th Cir. 1995) ("Rather than being inequitable ... allowing the trustee to [keep the purchased asset while giving the transferee no recovery for the purchase price] is really the only fair result for the other creditors."). The Decision and *Kingsley* reason that § 550's restorative policy requires courts to make initial transferees whole by granting a particular equitable remedy not provided in the Code – *i.e.,* improving initial transferees' claim priority by allowing them to reduce their § 550 liability on a dollar-for-dollar basis for the amount they paid the debtor.[14] App. 24a-25a; *Kingsley,* 518 F.3d at 877-78.

This reasoning directly conflicts with the rule established by this Court and the courts of appeals, which specifically precludes bankruptcy courts from granting equitable remedies that improve claim priority when other statutory remedies already exist. *See e.g., U.S. v. Noland*, 517 U.S. 535, 540-43 (1996) (general equitable principles cannot change § 507's IRS claim priority); *United States v. Sutton*, 786 F.2d 1305, 1307-08 (5th Cir. 1986) (equity cannot be used to allow payment of claim for unmatured spousal and child support payments); *Southern Ry. Co. v. Johnson*

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[14] Such a reduction of § 550 liability improves a transferee's payment priority because it allows him to retain a portion of a property's value for his own exclusive benefit to the detriment of the other unsecured creditors, who would share in that value without the reduction in the transferee's liability.

Bronze Co., 758 F.2d 137, 141-42 (3rd Cir. 1985) (equity cannot support improvement of priority for contractual indemnification claim); *see also Norwest Bank Worthington v. Ahlers*, 485 U.S. 197, 206 (1988) (equitable powers may be exercised only within Code's confines).

It also directly conflicts with the results of those cases that discuss § 550's restorative policy. Those cases limit the transferees of avoidable transfers to their statutory remedy – *i.e.*, the filing of an unsecured claim – rather than providing them with a reduction in their § 550 liability. *See e.g., In re Trout*, 609 F.3d 1106, 1114 (10th Cir. 2010) ("[a]fter avoidance of the lien, the estate once again had a depreciating asset *and an unsecured obligation to the lender*") (emphasis added); *In re Taylor*, 599 F.3d 880, 884, 891-93 (9th Cir. 2010) (while estate recovered transferred property, transferee received only an unsecured claim for the loan amount); *Wells Fargo Home Mort., Inc. v. Lindquist*, 592 F.3d 838, 846 (8th Cir. 2010) (estate recovered judgment for transferred property's value, but transferee received only an unsecured claim for the loan amount).

Further, the Decision also relies on a novel belief that § 550 silently incorporates the defense provided in § 548(c) because § 544(b) and § 548 transferees must be subject to symmetrical recoveries. App. 25a. There is no stated basis for this belief. In fact, the belief contradicts the plain meaning of § 548(c)'s opening clause. That clause expressly disavows any symmetry between the treatment of § 544 and § 548 transferees. It states that § 548(c) applies "*except to the extent that a transfer ... is voidable under section 544.*" If Congress truly intended to extend § 548(c)'s

protections to § 544(b) transferees, it would have done so expressly, as it did in 1998 when it added § 544(b)(2) as a new provision to extend § 548(a)(2)'s protection to § 544(b) transferees. As a different Ninth Circuit panel cautioned, courts should not interpret either § 544 or § 548 with the other in mind because each section presents a "separate and distinct method of avoidance" that renders the other section "completely irrelevant." *In re Acequia*, 34 F.3d 800, 810-11 (9th Cir. 1994).

Finally, the Decision's assumption that § 550 incorporates § 548(c)'s protections and applies them to those transfers avoided under other sections would render § 548(c) superfluous. In *Boyer-III*, the Seventh Circuit considered[15] and rejected the assumption when it affirmed *Boyer-II*. *Boyer-II*, 2009 WL 418275 *17, *aff'd* 587 F.3d 787. In this respect, *Boyer-III* adopted this Court's "deep reluctance to interpret a provision so as to render superfluous other provisions in the same enactment." *Pennsylvania Dept. of Public Welfare v. Davenport*, 495 U.S. 552, 562 (1990) (Code).

II. THE CIRCUITS ARE NOW IN CONFLICT OVER THE DEFINITION OF "VALUE" IN § 550.

The Decision applies § 550 so that "value" means a property's *reasonably equivalent value*. It is in *direct conflict* with the decisions of this Court and the courts of appeals, which hold that "value" means either a property's *fair market value* or, in very limited cases,

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[15] Appellee/Cross-Appellant's Brief to the Seventh Circuit Court of Appeals, 2009 WL 1900130 at Section VII., Argument VIII.

its foreclosure sale price. Because the Decision is erroneous, it allows Respondent to escape liability for more than $9,000,000 (the $5,327,185 difference between the Properties' *fair market value* and the Parcels' *reasonably equivalent value*, plus the 7% annual prejudgment interest awarded by the bankruptcy court). This amount should be made available for equitable distribution to all of JTS's creditors rather than retained by Respondent.

A. The Decisions Of This Court And Other Courts Hold That, Throughout The Code And In § 550, "Value" Means A Property's *Fair Market Value* Or Its Foreclosure Sale Price.

This Court has found that "value," as used in the Code, means either a property's *fair market value* when the property is subject to a fair market, or its foreclosure sale price when the property was sold at a properly conducted foreclosure. *BFP*, 511 U.S. 531. In *BFP*, this Court analyzed the term "value" as part of § 548's phrase "reasonably equivalent value." The Court broke down the phrase into two separate terms – "reasonably equivalent" and "value." *BFP*, 511 U.S. at 538 n.4. It found that "value" means a property's worth under one of two particular market conditions – *i.e.*, either a fair market[16] or a market in which the

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[16] The Court described *fair market value* as a "well-established concept" meaning the price fixed in a fair market, which this court defined as:

> not the price which might be obtained on a sale at public auction or a sale forced by the necessities of the owner, but such a price as would be fixed by negotiation and mutual agreement, after ample time to find a purchaser,

property is subject to a properly conducted foreclosure sale. *Id.* at 538-39. After holding that "value" means the foreclosure sale price in the foreclosure context, *Id.* at 545-46, it noted that in "the vast majority of cases" when property is not subject to foreclosure, "value" means a property's *fair market value*. *Id.* at 548.

This Court defined "value" similarly in *American Commercial Corp. v. Rash*, 520 U.S. 953 (1994). In *Rash*, this Court held that "value," as used in § 506(a), means *fair market value* when it refers to property that is not subject to foreclosure or cannot be sold at foreclosure due to the Code's protections.[17] *Rash*, 520 U.S. at 960, 962-64, 965 & n.6.

Based on *BFP* and *Rash*, "value" in § 550 must mean *fair market value* when it refers to property that is not and was not subject to foreclosure. *See Sullivan v. Stroop*, 496 U.S. 478, 484 (1990) ("identical words used in different parts of the same act are intended to have the same meaning"). This conclusion is supported by the cases in which courts applying § 550 have refused to award a property's value without

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> as between a vendor who is willing (but not compelled) to sell and a purchaser who desires to buy but is not compelled to take the particular ... piece of property.

Id. at 537-38, *citing Black's Law Dictionary*, 971 (6th ed. 1990).

[17] Instead of using the term *fair market value*, the Court used the term *replacement value*, which it found to have the same substantive meaning as *fair market value* – *i.e.*, "the price a willing buyer ... would pay a willing seller to obtain property of like age and condition." *Compare Rash*, 520 U.S. at 959 n.2, *with BFP*, 511 U.S. at 537-38.

sufficient evidence of *fair market value*.[18] *Taylor*, 599 F.3d at 890-91, 893, *quoting In re Brun*, 360 B.R. 669, 674 (Bankr. C.D. Cal. 2007) ("Typically, courts *equate 'value' with the fair market value* of the subject property at the time of the transfer") (emphasis added); *Trout*, 609 F.3d at 1112 (*dicta*), *quoting In re Bremer*, 408 B.R. 355, 360 (B.A.P. 10th Cir. 2009) ("When the record is devoid of evidence on the property's *market value* ... courts have ordered the property to be returned") (emphasis added); *In re King Arthur Clock Co.*, 105 B.R. 669, 672 (Bankr. S.D. Ala. 1989) (court stated "*value connotes market value*," and ordered transferee to return property because it lacked evidence to find market value) (emphasis added); *In re Vann*, 26 B.R. 148, 149 (Bankr. S.D. Ohio 1983) (same).

B. The Decision Is Erroneous And Conflicts Directly With The Above Cases. It Holds That "Value" In § 550 Means A Property's *Reasonably Equivalent Value*.

The Decision *directly conflicts* with this Court's decisions holding that "value" means either *fair market value* or foreclosure sale price depending on to which market a property was subject. After holding that the Transfer is a constructive fraudulent transfer under California law and void under § 544(b), App. 23a, the Decision went on to award Trustee the Properties' "value" under § 550. But instead of affirming the district court, which had interpreted

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[18] When Congress desires a different meaning for "value," it uses modifying terms and phrases. *See e.g.* 11 U.S.C. §§ 502(b)(4), 506(a), 522(a)(2), 548(a)(1)(B).

"value" as meaning the Properties' *fair market value* of $17,147,185, it awards the Parcels' *reasonably equivalent value* of $11,820,000, thus, necessarily, albeit implicitly, finding that "value" in § 550 means *reasonably equivalent value*. App. 11a-12a, 33a.

The Decision does not discuss *BFP*, *Rash*, or the other decisions that define value as *fair market value* in § 550 recovery actions. It does not acknowledge the conflict it is creating with this Court and other courts. Moreover, it does not explain how "value" possibly can mean *reasonably equivalent value* in a § 550 recovery context when: (1) it is a novel phrase, *BFP*, 511 U.S. at 537, that is used exclusively in an avoidance context to determine whether a transfer is a fraudulent transfer, *Id.* at 535; and (2) avoidance and recovery are distinct and separate concepts. *In re Burns*, 322 F.3d 421, 427 (6th Cir. 2003) (avoidance and recovery are separate functions), *citing* H.R.Rep. No. 95-595, at 375 (1977); *In re Int'l . Servs.*, 408 F.3d 689, 703 (same) (11th Cir. 2005); *In re Acequia,* 34 F.3d at 809 (same). Consequently, the Decision's finding that "value" means the Parcels' *reasonably equivalent value* in a recovery context creates a conflict that is unsupported.

III. The Circuits Are Now In Conflict Over Whether Settlement Credits Awarded Under § 550 Are Controlled Solely By Federal Procedure.

The Decision grants Respondent the Credit based on California procedure. It is in *direct conflict* with the decisions of this Court and the courts of appeals, which hold that only federal procedure controls whether to award a settlement credit to reduce liability for federal claims such as and including § 550. The Credit, as a

matter of law, could not have been awarded under federal procedure because the necessary federal criteria were not met. Because the Decision is erroneous, it allows Respondent to escape liability up to $4,500,000. This amount should be made available for equitable distribution to all of JTS's creditors rather than retained by Respondent.

A. The Decisions Of This Court And Other Courts Hold That The Awarding Of Settlement Credits To Reduce The Liability For Federal Claims, Such As and Including § 550, Are Controlled Solely By Federal Procedure.

Federal law controls remedial schemes enacted by Congress through its Constitutional powers, especially when there is a strong interest in national uniformity and state law could frustrate federal policy. *Kamen v. Kemper Financial Services, Inc.*, 500 U.S. 90, 98 (1991); *U.S. v. Kimbell Foods, Inc.*, 440 U.S. 715, 726-28 (1979). Of course, the interest in bankruptcy uniformity is recognized in the Constitution. U.S. Constitution Article I, Section 8, Clause 4. The importance of a uniform federal procedure has similarly been recognized by this Court. *Hanna v. Plumer*, 380 U.S. 460, 463 (1965) (certiorari granted because of the "threat to the goal of uniformity of federal procedure"). Thus, the courts of appeals reject the use of state procedure and, instead, apply federal procedure to determine whether to award settlement credits under § 550(d)'s single satisfaction rule. *In re Prudential of Florida Leasing, Inc.*, 478 F.3d 1291, 1298-99, 1301-02 (11th Cir. 2007), *citing Kamen* 500 U.S. 90; *Kimbell Foods*, 440 U.S. 715; *Bowers v. Kuse Enters., Inc.*, 1998 WL 957455, at *7 (4th Cir.

1998); *In re Lendvest*, 42 F.3d 1181, 1184 (9th Cir. 1994).

Prudential of Florida is particularly applicable because it discusses at length the application of *Kamen* and *Kimbell Foods* in the context of both § 550 and Florida law, which, like California law, allows a full settlement credit for unallocated settlement payments. The Eleventh Circuit found that § 550(d)'s single satisfaction rule renders state procedure regarding settlement credits inapplicable because state law could frustrate the important bankruptcy policies of: (1) promoting equitable distribution of a bankruptcy estate's assets; (2) preventing the depletion of bankruptcy estates; and (3) protecting bankruptcy creditors who advanced credit in ignorance of fraud. *Id.* at 1297-99, 1301-02. It also noted that "a uniform rule of federal law is preferable because the rule of single satisfaction concerns the judicial *process* necessary to approve settlements that terminate bankruptcy proceedings and the valuation of settled claims in collateral litigation." *Id.* at 1299 (original emphasis).

The single satisfaction rule applied under federal procedure does not base a non-settling defendant's credit on the amount of settlement paid by settling defendants. *McDermott, Inc. v. AmClyde*, 511 U.S. 202, 221 (1994) ("[non-settling defendants] are not entitled to a reduction in liability when the plaintiff negotiates a generous settlement"). Instead, the non-settling defendant's settlement credit is determined by a judicial finding of his proportionate share of liability. *Id.* at 218-20. As the *McDermott* Court stated: "a plaintiff's good fortune in striking a favorable bargain with one defendant gives other defendants no claim to

pay less than their proportionate share of the total loss." *Id.* at 220.

To determine a non-settling defendant's proportionate share of liability under federal procedure, courts, at the time of trial, must: (1) *find joint liability* between settling and non-settling defendants; and (2) *allocate culpability* between the jointly liable defendants. *McDermott*, 511 U.S. at 216-17 ("the relative fault of the parties will have to be determined"); *U.S. Industries, Inc. v. Touche Ross & Co.*, 854 F.2d 1223, 1235 n.17 (10th Cir. 1988) (federal common law requires finding of settling defendants' joint liability); *Lendvest*, 42 F.3d at 1184 (no equitable right to settlement credit without joint liability); *Wren v. Spurlock*, 798 F.2d 1313, 1323 n.3 (10th Cir. 1986) (joint liability is required), *citing Northwest Airlines, Inc. v. Transport Workers*, 451 U.S. 77, 83, 87-88 (1981); *Dobson v. Camden*, 725 F.2d 1003, 1005-06 (5th Cir. 1984) (*en banc*) (requires finding settling defendants' jointly liable on the claim for which non-settling defendant is liable). Without these findings and allocations, there can be no settlement credit under federal law.

B. The Decision Is Erroneous And Conflicts Directly With The Above Cases. It Holds That Respondent Properly Received A Settlement Credit To Reduce His § 550 Liability Based On State Procedure.

Reversing the district court, the Decision awarded Respondent the Credit based solely on California procedure. App. 25a-33a. In this respect, it conflicts directly with the above cases, which applied federal procedure to award settlement credits to reduce

liability for federal claims such as § 550. Moreover, the Decision ran afoul of the Settlement Order, which incorporated the federal criteria of joint liability and culpability. App. 122a.

Had the Decision applied federal procedure, it would have had to deny the Credit because neither of the federal criteria for a settlement credit was met. First, the bankruptcy court never allocated liability. App. 32a. Second, it never found joint liability.[19] In fact, as a matter of law, there could not have been a finding of joint liability because the settling defendants were not transferees. And § 550 does not extend liability to non-transferees regardless of whether they conspired with or aided and abetted actual transferees. *Robinson v. Watts Detective Agency, Inc.*, 685 F.2d 729, 738 (1st Cir. 1982) (Act case), *citing Klein v. Tabatchnick*, 610 F.2d 1043, 1048 n.4 (2nd Cir. 1979); *Jackson v. Star Sprinkler Corp.*, 575 F.2d 1223, 1234 (8th Cir. 1978) (Act case); *In re Christian & Porter Aluminum Co.*, 584 F.2d 326, 339 (9th Cir. 1978) (Act case); *In re Hamilton Taft & Co.*, 176 B.R. 895, 902 (Bankr. N.D. Cal. 1995) (Code case), *aff'd on other grounds* 114 F.3d 991 (9th Cir. 1997), *citing Elliott v. Glushon*, 390 F.2d 514, 516 (9th

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[19] Without citing to the record, the Decision states that the bankruptcy court made an oral finding of joint liability. App. 32a. The bankruptcy court's only oral reference to the settling defendants' joint liability was its mention that Trustee had alleged that settling defendants were jointly liable for the Transfer. *See* footnotes 6 and 7, *infra*. As a matter of law, this would not constitute the necessary finding of joint liability. *Touche Ross*, 854 F.2d at 1227 n. 20 (critical focus of joint liability is on actual finding rather than allegations existing at time of the settlement).

Cir.1967) (Act case). The Decision fails to discuss the above cases because it focused almost exclusively on California procedure. Thus, the granting of the Credit conflicts directly with those cases that find federal procedure exclusively controls federal claims, such as and including §550, and requires both a finding of joint liability and an allocation of culpability.

IV. THE QUESTIONS PRESENTED ARE IMPORTANT.

In addition to its obvious importance to the parties (who have tens of millions of dollars at stake) that the issues in this matter be correctly decided, resolution of the intercircuit conflicts in this matter is important because of the heightened need for uniformity in the areas of bankruptcy and federal procedure. *See United States Constitution,* Article I, Section 8, Clause 4 (bankruptcy uniformity mandated); *Hanna*, 380 U.S. at 463 (importance of uniform federal procedure). The need for bankruptcy uniformity makes certiorari appropriate when conflicts involve: (1) as few as two circuits, *see e.g., City of New York v. Saper*, 336 U.S. 328, 341 (1949); (2) a single term used in multiple Code sections, *see e.g., Begier v. I.R.S.*, 496 U.S. 53, 57 n.2 (1990); or (3) the particular bankruptcy issues raised in this matter – *i.e.*, avoidance, recovery, and claim priority. *See e.g., Wolas*, 502 U.S. at 153-54 (preference avoidance and recovery); *Howard Delivery*, 547 U.S. at 657 (claim priority).

Furthermore, the importance of correctly interpreting a single Code section goes well beyond that particular section because the interpretation will impact the methodology established by this Court to achieve a predictability of interpretation. As the

dissenting opinion in *Dewsnup v. Timm*, 502 U.S. 410 (1992), warned:

> The principal harm caused by today's decision is not the misinterpretation of §506(d) of the Bankruptcy Code.... The greater and more enduring damage [of such opinions is the] destruction of predictability, in the Bankruptcy Code and elsewhere. By disregarding well-established and oft-repeated principles of statutory construction, it renders those principles less secure and the certainty they are designed to achieve less attainable.

Id. at 435 (Scalia, J., joined by Souter, J., dissenting).

Emphasizing the above point, the concurring opinion in *Bank of America Nat. Trust & Sav. Ass'n v. 203 North LaSalle*, 526 U.S. 434 (1999), stated:

> The majority also underestimates the need for a clear method for interpreting the Bankruptcy Code....
>
> ***
>
> The risks of relying on [improper methodology] in interpreting the Bankruptcy Code, which seeks to bring an entire area of law under a single, coherent statutory umbrella, are especially weighty.

Id. at 460-61 (Thomas, J., joined by Scalia, J., concurring).

Additionally, it is essential to resolve these conflicts between the Decision and the many decisions of this Court and the courts of appeals because the conflicts are outcome-determinative. *See,* A. Hellman, *Light On A Darkling Plain: Intercircuit Conflicts In The Perspective Of Time And Experience*, 1998 Sup. Ct. Rev. 247, 252-53 (1998) (outcome-determinative conflicts are intolerable). And unresolved outcome-determinative intercircuit conflicts necessarily result in unequal treatment of parties based on nothing more than venue, thus creating incentive for forum shopping.

Finally, because the issues here are not fact sensitive, this case provides this Court with what may be its best opportunity to completely and finally resolve these conflicts using broad rules that will apply under any fact pattern. Such a broad resolution of the conflicts will help relieve an overburdened judicial system by increasing the predictability that guides: (1) lower courts when they construe the Code; (2) lawyers when they formulate strategy: and (3) parties when they must decide whether to file cases or settle litigation. *See,* M.Cordray and R.Cordray, *The Philosophy of Certiorari: Jurisprudential Considerations in Supreme Court Case Section*, 82 Wash. U.L.Q. 389, 428-29 (2004); *see e.g., Laing v. U.S.*, 423 U.S. 161, 167 (1976) (certiorari was warranted to review a conflict when "some 70 pending cases in the federal courts depended on its resolution"). The need to relieve the judicial system is amplified here because § 550 applies in all bankruptcy cases regardless of chapter, and bankruptcy case filings continue to increase rapidly. *See* www.uscourts.gov/Statistics/Bankruptcy Statistics.aspx (1,572,597 new

bankruptcies filed between June 30, 2009 and 2010, which represents a 20.4% annual increase).

CONCLUSION

This petition for a writ of certiorari should be granted.

Dated: January 12, 2011

Respectfully submitted,

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APPENDIX

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APPENDIX A

FOR PUBLICATION
UNITED STATES COURT OF APPEALS
FOR THE NINTH CIRCUIT

[Filed August 10, 2010]

No. 07-15970 / D.C. No. CV-05-04709-JF

In the Matter of: JTS CORPORATION,

Debtor,

SUZANNE L. DECKER,
Plaintiff-appellee,

V.

JACK TRAMIEL,
Defendant-appellant,

and

ROGER W. JOHNSON; JEAN D. DELEAGE; AMBER ARBITRAGE LDC, A Private Investment Fund Incorporated in the Cayman Islands,
Defendants,

OFFICE OF THE U.S. TRUSTEE,
Trustee,

LIP-BU TAN,
Third-party-defendant.

No. 07-16004 / D.C. No. CV-05-04709-JF

In the Matter of: JTS CORPORATION,

Debtor,

SUZANNE L. DECKER,
Plaintiff-appellee,

V.

JACK TRAMIEL,
Defendant-appellant,

and

ROGER W. JOHNSON; JEAN D. DELEAGE; AMBER ARBITRAGE LDC, A Private Investment Fund Incorporated in the Cayman Islands,
Defendants,

OFFICE OF THE U.S. TRUSTEE,
Trustee,

LIP-BU TAN,
Third-party-defendant.

OPINION

Appeal from the United States District Court
for the Northern District of California
Jeremy D. Fogel, District Judge, Presiding

Argued and Submitted
November 6, 2009—San Francisco, California

Filed August 10, 2010

Before: Procter Hug, Jr., Pamela Ann Rymer, and
M. Margaret McKeown, Circuit Judges.

Opinion by Judge Hug

COUNSEL

Christian B. Nielsen, San Jose, California, and G. Larry Engel, Morrison & Foerster LLP, San Francisco, California, for the appellant.

Jeffrey C. Wurms, Wendel, Rosen, Black & Dean, LLP, Oakland, California, for the appellee.

OPINION

HUG, Circuit Judge:

This case involves a bankruptcy appeal. Appellant Jack Tramiel, a member of the JTS Corporation board of directors, attempted to assist the debtor, JTS Corporation ("JTS"), and purchased real property from JTS. It was held that this purchase was a constructive fraudulent conveyance and that Tramiel was liable for

the value of the property. The major issues in this case are what the fair market value of the real property is, whether Tramiel is entitled to an offset for the value he paid for the property as a good faith transferee, and whether Tramiel is entitled to a credit for the amount that his codefendants paid in a settlement agreement. We have jurisdiction under 28 U.S.C. § 158(d)(1), and we affirm.

I. Factual Background

In 1994, JTS Corporation ("JTS") was formed to design, manufacture, and market hard disks for personal computers. By 1996, after a contract with JTS was terminated, JTS needed additional working capital to continue. At that time, JTS determined that it was not able to go public to acquire the additional funds that it needed and agreed to merge with Atari Corporation ("Atari") to obtain the funds. Through the merger, JTS received $15 million in cash, $55 million in intellectual property, eight separate real properties located in California and Texas, and a $25 million loan which JTS hoped would carry it through September 1996. In addition, Tramiel, the defendant, who was the chairman of Atari's board of directors, was brought onto the JTS board of directors.

Since the funds acquired through the merger were only intended to carry JTS through September, Virginia Walker, JTS's chief financial officer, began to search for additional capital. After Walker failed to secure funds from several banks, she approached Tramiel and suggested that he buy the eight separate real properties ("real property") that JTS would acquire as a result of the Atari merger. In response, Tramiel suggested that he buy the real property for

$10 million and permit JTS to retain an option to repurchase the real property for the same $10 million for one year. If JTS exercised the option, Tramiel would keep the greater of $1 million or the rental income generated by the property for a one-year period.

In June 1996, JTS's board of directors approved the sale of the real property to Tramiel and authorized Walker to work with an attorney to implement the sale. Evidence showed that the JTS board believed that the real property sale to Tramiel was the quickest way of raising the necessary funds to keep the company running and that the repurchase option would allow a year to regain the real property if it decided to do so. One director recalled a discussion that although JTS might receive a greater price for the real property under other circumstances, in light of the immediate need for funds, Tramiel's offer was fair. Tramiel removed himself from the boardroom and abstained from all voting during the sale discussions. By July 1996, JTS's debt exceeded its assets by $23 million. In September 1996, the real property sale closed. Still struggling, JTS liquidated other property acquired from the merger. Despite these and other efforts, JTS was unable to recover and in November 1998, was forced into bankruptcy through an involuntary petition. Later, JTS filed a Chapter 11 petition, scheduling assets of $4.2 million and liabilities of $136 million. In 1999, the case converted to Chapter 7.

II. Procedural Background

In 2003, the trustee, Suzanne L. Decker filed a complaint against JTS's directors (including Tramiel),

its attorneys, and a shareholder, alleging fraudulent conveyance and other claims. In 2004, Tramiel's co-defendants, *i.e.*, the attorney defendants and two members of the JTS board of directors, reached a settlement with Decker in which they agreed to pay the JTS bankruptcy estate $4.5 million. The bankruptcy court issued an order approving the settlement and trial proceeded against only Tramiel.

In 2005, the bankruptcy court held *inter alia* that the sale of the real property to Tramiel was avoided as a constructive fraudulent conveyance under 11 U.S.C. § 544(b) of the Bankruptcy Code and California Civil Code § 3439.04. The bankruptcy court stated that under § 544(b) a trustee may avoid transfers of a debtor's property that would be avoidable under state law. Under California Civil Code § 3439.04, a transfer is avoidable if the debtor completed the property transfer without receiving a reasonably equivalent value in exchange for the property and the debtor intended to incur or believed or reasonably should have believed that it would incur debts beyond its ability to pay. In determining reasonably equivalent value, the bankruptcy court found that the fair market value of the eight separate real properties which Tramiel bought from JTS was $15,760,000 if the properties had been individually exposed to the market for one year and sold separately. Because the property was sold as a bundled portfolio and it was a quick sale, the court held that a 5% reduction should apply for a quick sale and a 20% reduction should apply for a bundled sale. Thus, the bankruptcy court held that the reasonably equivalent value of the real property was $11,820,000.

The bankruptcy court determined that the value of the option to repurchase the real property was $432,815. The bankruptcy court stated that the value of the repurchase option is determined by subtracting the strike price of the repurchase option from the fair market value of the real property. The bankruptcy court held that the stated strike price, $10 million, should be added to the loss of rental income for the real property for one year, which was $1,387,185, to equal a total $11,387,185 strike price. The bankruptcy court subtracted the strike price of $11,387,185 from the reasonably equivalent value of the real property, *i.e.*, $11,820,000, and held that the value of the repurchase option was $432,815. The bankruptcy court held that Tramiel paid a total consideration of $10,432,815 for the real property by adding the value of the repurchase option to the $10 million purchase price.

In addition, the bankruptcy court held Tramiel was a good faith transferee under California Civil Code § 3439.08(d)(3). The bankruptcy court determined that under California Civil Code § 3439.07(a)(1) the ability of a trustee to avoid a transfer is subject to the limitations under California Civil Code § 3439.08. Under § 3439.08(d)(3), a good faith transferee is entitled to a reduction in liability to the extent of the value given to the debtor. The bankruptcy court held that Tramiel was a good faith transferee entitled to a reduction of the $10 million consideration paid for the real property plus the value of the repurchase option, *i.e.*, $432,815. The bankruptcy court held that subtracting the good faith transferee reduction of $10,432,815 from the $11,820,000 reasonably equivalent value left Tramiel with a liability of $1,387,185. After determining that Tramiel was not

entitled to a settlement credit, the bankruptcy court held that Tramiel's liability was $1,387,185 plus interest.

Tramiel filed a motion in bankruptcy court to amend the judgment in order to grant him a settlement credit under California Civil Procedure Code § 877. The bankruptcy court amended its judgment and held that Tramiel was entitled to a settlement credit against his liability in the amount paid by the settling defendants to the bankrupt estate, *i.e.*, $4.5 million. Because this settlement credit exceeded Tramiel's liability, the bankruptcy court held that Decker could not recover any amount from Tramiel.

On appeal, the district court affirmed in part and reversed in part the bankruptcy court's judgment. The district court affirmed the bankruptcy court's determination that Tramiel was liable for constructive fraudulent conveyance under § 544(b) and § 3439.04(a). The district court held, however, that the fair market value of the real property was $15,760,000 and the rents were $1,387,185, creating a total fair market value of $17,147,185 for the real property. Unlike the bankruptcy court, the district court concluded that the appropriate measure of liability is the fair market value.

The district court affirmed the bankruptcy court's determination that Tramiel was a good faith transferee under California Civil Code § 3439.08(d)(3) and thus reduced his liability by $10,432,815, *i.e.*, the $10 million purchase price and value of the repurchase option, $432,815. The district court subtracted $10,432,815 from the fair market value of the real

property, *i.e.*, $17,147,185, and held that Tramiel's liability was $6,714,370.

The district court reversed the bankruptcy court's holding that Tramiel was entitled to a settlement credit of the $4.5 million paid by his co-defendants. The district court held that under California Civil Procedure Code § 877, a settlement bars nonsettling defendants from seeking contribution from the settling defendants, but the nonsettling defendant's liability may be reduced by the settlement amount if all of the defendants are joint tortfeasors. The district court held that Tramiel was not a joint tortfeasor because (1) there was no evidence that Tramiel had requested a finding of joint liability; (2) the written settlement agreement between the co-defendants and bankrupt estate allocated liability for each co-defendant for certain torts and did not address the fraudulent conveyance; and (3) the written settlement agreement contained an integration clause, stating that the agreement was the complete expression of the parties' intent. Thus, the district court held that Tramiel was liable for the fraudulent conveyance in the amount of $6,714,370.

III. Discussion

A. Standard of Review

We review de novo a district court's decision on appeal from a bankruptcy court. *In re Greene*, 583 F.3d 614, 618 (9th Cir. 2009). We apply the same standard of review applied by the district court. *Id.* We review a bankruptcy court decision independently and without deference to the district court's decision. *In re Strand*,

375 F.3d 854, 857 (9th Cir. 2004). "The bankruptcy court's findings of fact are reviewed for clear error, while its conclusions of law are reviewed de novo." *Id.* (citing *Galam v. Carmel (In re Larry's Apt., L.L.C.)*, 249 F.3d 832, 836 (9th Cir. 2001)). We must accept the bankruptcy court's findings of fact, unless "the court is left with the definite and firm conviction that a mistake has been committed." *Greene*, 583 F.3d at 618. "Mixed questions of law and fact are reviewed de novo." *In re Chang*, 163 F.3d 1138, 1140 (9th Cir. 1998).

B. Fraudulent Conveyance & Value of Real Property

[1] Tramiel argues that the district court erred when it determined with regard to the fraudulent conveyance claim that the value of the real property was its fair market value $17,147,185. Under § 544(b)(1) of the Bankruptcy Code, a "trustee may avoid any transfer of an interest of the debtor in property or any obligation incurred by the debtor that is voidable under applicable law." Under California Civil Code § 3439.04(a), a transfer is avoidable if the debtor made the transfer without receiving a reasonably equivalent value in exchange for the transfer and the debtor intended to incur, or believed or reasonably should have believed that it would incur debts beyond its ability to pay as they became due. Reasonably equivalent value is the value of the property on the date of the transfer from the perspective of the creditors. *In re Prejean*, 994 F.2d 706, 708 (9th Cir. 1993); *In re Fairchild Aircraft Corp.*, 6 F.3d 1119, 1125-26 & n.5 (5th Cir. 1993). Courts may consider the fair market value or what would be the fairly equivalent value of the property, taking into

consideration all of the specific circumstances of each case affecting the value of the asset. *Hansen v. Cramer*, 245 P.2d 1059 (Cal. 1952); *Bailey v. Leeper*, 298 P.2d 684 (Cal. Ct. App. 1956). A finding of what constitutes the value of real property is a finding of fact which may be reversed only if it is shown that it was clearly erroneous. *In re Arnold*, 85 F.3d 1415, 1421 (9th Cir. 1996); *In re Tuma*, 916 F.2d 488, 491 (9th Cir. 1990).

[2] In this case, we conclude that the district court erred in holding that the fair market value which it fixed at $17,147,185 was determinative. The bankruptcy court's finding that the reasonably equivalent value was $11,820,000 was not clearly erroneous. The bankruptcy court found that the fair market value of the property was $15,760,000 without applying quick and bundled sale reductions. Both parties' experts agreed that $15,760,000 would be the value of the property if it had been sold individually and exposed to the market for a year and that this was thus an appropriate starting point. The bankruptcy court then applied reductions of 5% for a quick sale and 20% for a bundled sale to the $15,760,000, reducing the fair market value to $11,820,000 (the reasonably equivalent value). This was not clearly erroneous. Evidence showed that JTS wanted immediate cash and was willing to take a reduced price for the real property to obtain the funds quickly. JTS wanted a quick and bundled sale and even Decker's expert agreed that reductions for a quick and bundled sale were proper if a seller required those terms. For a bundled sale, Tramiel's expert testified that a 20 to 30% reduction was proper and Decker's expert testified that a 5.5% reduction was proper. The bankruptcy court found Tramiel's expert more

persuasive and imposed the lowest percentage that he recommended. For a quick sale, Decker's expert testified that if a discount was applied that he would apply 1% per month, *i.e.*, a total of five percent. The bankruptcy court applied this percentage. No evidence shows that the bankruptcy court's reasonably equivalent value determination of $11,820,000 was clearly erroneous. Accordingly, we disagree with the district court's determination based entirely on fair market value, and affirm the bankruptcy court's reasonably equivalent value determination. *In re Tuma*, 916 F.2d at 491 (holding bankruptcy judge's determination was not clearly erroneous even though there were many different methods of determining value); *Sammons v. Comm'r*, 838 F.2d 330, 334 (9th Cir. 1988) (holding court did not abuse its discretion in rejecting certain appraisals regarding valuation); *Anderson v. City of Bessemer City, N.C.*, 470 U.S. 564, 574 (1985) (stating if there are two views of the evidence, a court's choice between them is not clearly erroneous). Accordingly, we hold, as the bankruptcy court held, that the reasonably equivalent value of the real property was $11,820,000.

[3] The bankruptcy court also did not clearly err in determining that the fair market value of the repurchase option was $432,815. The question of whether JTS received a reasonably equivalent value also turns on the value of the repurchase option that Tramiel gave to JTS. Tramiel's expert correctly testified that the value of the repurchase option was the difference between the reasonably equivalent value of the property and the fixed strike price. *See In re Calvillo*, 263 B.R. 214 (W.D. Tex. 2000). Here, the bankruptcy court properly concluded that the strike price was $10 million plus $1,387,185 for rents, for a

total of $11,387,185. Subtracting that total from the reasonably equivalent value of $11,820,000 equaled a total of $432,815 for the value of the repurchase option. Because there is no evidence that this determination was clearly erroneous, the bankruptcy court properly found that the value of the repurchase option was $432,815.

C. Good Faith Transferee

Decker argues that the bankruptcy and district courts erred by holding that Tramiel was a good faith transferee under California Civil Code § 3439.08(d)(3) and reducing his liability by the value he paid for the property, *i.e.*, $10,432,815. Decker argues that § 544(b) and § 550(a) claims are only subject to state laws that determine voidability. Decker argues that § 3439.08(d)(3) does not determine voidability and is therefore inapplicable to § 544(b) and § 550(a) claims.

i. Sections 544 and 550 of the Bankruptcy Code

[4] Under § 544(b) and § 550(a) of the Bankruptcy Code, a trustee may avoid a fraudulent transfer of property if that transfer is voidable under applicable state law. *In re United Energy Corp.*, 944 F.2d 589, 593 (9th Cir. 1991). Fraudulent transfer law has been a part of debtor-creditor relations since 1571. 5 *Collier on Bankruptcy* § 548.01[1][a], [b] at 548-8, 11 (Alan N. Resnick & Henry J. Sommer 16th Ed.). Such laws were enacted to allow a creditor to avoid an improper transaction by a debtor who attempts to unjustly reduce assets and avoid his creditors' claims. *Id.* Prior to 1938, however, federal bankruptcy law only addressed a small number of fraudulent transfer cases in which there was actual intent to defraud and the

transfer occurred within four months of the bankruptcy. *Id.* at 548-11-12. In 1938, Congress enacted amendments to the Chandler Act and fully absorbed fraudulent transfer laws into federal bankruptcy law. *Id.* These 1938 amendments "brought the full panoply of fraudulent transfer law into federal law, including the ability to avoid constructively fraudulent transfers." *Id.* "Given the elemental nature of fraudulent transfer law, however, there was no preemption [of states] intended, and states (as well as the federal government) continued to adapt parts of fraudulent transfer law for their own purposes." *Id.* at 548-12.

Sections 548 and 544 of the Bankruptcy Code were enacted by Congress to allow a trustee the option of avoiding a fraudulent transfer under either state law or federal law. Section 548 was adopted in 1978. Section 548 allows a trustee to avoid a transfer if it is made within two years of filing a bankruptcy petition and the debtor either had actual intent to defraud or received less than reasonably equivalent value in exchange for the transfer. 11 U.S.C. § 548(a)(1)(A), (B). Subsection (c) of § 548 provides that a trustee's recovery may be reduced by the value given for the transfer if the transferee made the transfer in good faith.

In 1978, § 544 of the Bankruptcy Code was enacted in recognition of the growth of state fraudulent transfer laws. *Collier on Bankruptcy* § 548.01[2] at 548-12. Section 544 enables a bankruptcy trustee to avoid any transfer of property that an unsecured creditor with an allowable claim could have avoided under applicable state law. 11 U.S.C. § 544(b)(1); Alan Resnick, *Finding the Shoes That Fit: How Derivative*

is the Trustee's Power to Avoid Fraudulent Conveyances Under Section 544(b) of the Bankruptcy Code?, 31 Cardozo L. Rev. 205 (2009). The purpose of this section was to recognize the body of state laws addressing fraudulent transfers and allow a trustee the choice of avoiding transfers under § 544 and the applicable state fraudulent transfer law, or under only federal law pursuant to § 548. *Collier on Bankruptcy* § 548.01[2] at 548-12.

[5] Section 550 of the Bankruptcy Code authorizes a trustee, after avoiding a fraudulent transfer under § 544 or § 548, to recover the property transferred or the value of the property for the benefit of the bankrupt estate. 11 U.S.C. § 550(a). Section 550(a) provides that "to the extent that a transfer is avoided under section 544 . . . [or] 548 . . . the trustee may recover, for the benefit of the estate, the property transferred, or, if the court orders, the value of such property." The purpose of § 550 is "to restore the estate to the financial condition it would have enjoyed if the transfer had not occurred." *In re Acequia*, 34 F.3d 800, 812 (9th Cir. 1994) (internal quotation marks omitted). The primary goal is equity and restoration, *i.e.*, "putting the estate back where it would have been but for the transfer." *Collier on Bankruptcy* § 550.02[3][a] at 550-10; 11 U.S.C. § 550(e)(1)(A); *In re Integra Realty Res., Inc.*, 354 F.3d 1246, 1266 (10th Cir. 2004); *In re American Way Serv. Corp.*, 229 B.R. 496, 530-31 (Bankr. S.D. Fla. 1999). Abiding its equitable underpinnings, a trustee's recovery under § 550 is limited if the transferee took the transfer for value in good faith without knowledge of its voidability. 11 U.S.C. § 550(b)(1). A good faith transferee is also permitted under § 550 to recover the value of any

improvements that were made after the transfer. 11 U.S.C. § 550(e)(1)(A).

ii. Cases Involving Sections 544 and 550

[6] The Supreme Court and this court have interpreted claims under § 544 and § 550 of the Bankruptcy Code to require that once avoidance is shown, the trustee's recovery cannot be limited in certain situations. *In Moore v. Bay*, 284 U.S. 4, 5 (1931), the Supreme Court addressed whether a bankruptcy trustee's recovery was limited on a fraudulent transfer claim under § 70e of the Bankruptcy Act, the precursor to § 544 of the Bankruptcy Code.[1] 11 U.S.C. § 110e (1976) (repealed); 11 U.S.C. § 544(b), Notes (stating § 544(b) is derived from former § 70e and that § 544(b) follows the rule of *Moore v. Bay*); *Sherwood Partners, Inc. v. Lycos, Inc.*, 394 F.3d 1198, 1201 (9th Cir. 2005) (stating that § 70e is the precursor of § 544(b)). In *Moore*, the "bankrupt executed a mortgage of automobiles, furniture, show room and shop equipment" and later recorded the mortgage. 284 U.S. at 4. Under California Civil Code § 3440, a transfer of personal property made by one who has the property and does not immediately deliver it, was void against those who were creditors at the time of the transfer and those who became creditors while the transferor still possessed the property.

---

[1] Section 70e(1) provided that a "transfer made or suffered or obligation incurred by a debtor adjudged a bankrupt under this Act which, under any Federal or State law applicable thereto, is fraudulent as against or voidable for any other reason by any creditor of the debtor, having a claim provable under this Act, shall be null and void as against the trustee of such debtor." *Miller v. Sulmeyer*, 263 F.2d 513, 515 (9th Cir. 1959)

Because of § 3440's application, the mortgage was void against creditors who were such on the date of the mortgage and those who became creditors between the date of the mortgage and the date it was recorded. *Id.* at 4-5. The Supreme Court, thus, had to address the issue of whether the mortgage was also void against creditors who gave the bankrupt credit after the date the mortgage was recorded. *Id.* at 5.

The Supreme Court held that for fraudulent transfer claims asserted by a bankruptcy trustee under § 70e "the right of the trustee to recover is dependent upon just one creditor with a cause of action and [is] not dependent at all upon the size of the creditor's claim against the debtor." *Collier on Bankruptcy* § 544.06[4] at 544-23. The Supreme Court held that a trustee could "avoid an entire transfer without regard to the size of the claim of the unsecured creditor whose rights and power the trustee [is] asserting." Helen Ryan Frazer, Laurel R. Zaeske, and Lynda T. Bui, *Fraudulent Transfer: Litigation Under the Bankruptcy Code and State Law*, 29 Cal. Bankr. J. 255, 269 (2007) (internal quotation marks omitted). "In other words, an entire transfer can be set aside even though the creditor's claim is nominal and, moreover, the recovery of the trustee is for the benefit of all creditors including those who had no right to avoid the transfer." *Id.* (internal quotation marks omitted). Thus, the Supreme Court held that the creditor with a cause of action under § 70e would share any recovery equally with unsecured creditors who otherwise could not recover. *Moore*, 284 U.S. at 5.

Following the rule of *Moore v. Bay*, in *Miller v. Sulmeyer*, 263 F.2d 513, 516 (9th Cir. 1959) we held that a bankruptcy trustee asserting a claim under

§ 70e of the Bankruptcy Act could recover on a chattel mortgage even though under California Civil Code § 2957 the mortgage was void as against any creditor after the date that the mortgage was recorded. In *Miller*, the Millers sold a business to the now bankrupt Delcon Corporation. *Id.* at 514. In return, the Millers "took back from Delcon a purchase money mortgage on chattels transferred to Delcon." *Id.* The Millers did not record the mortgage for 79 days. *Id.* A creditor filed a claim against the mortgage for $8,906.95 during that time. *Id.* The Millers later foreclosed on the mortgage, repossessed the chattel under the terms of the mortgage, and resold the property for $82,500. *Id.* Delcon was bankrupt at the time of the sale. *Id.*

Under California Civil Code § 2957, the mortgage and the Miller's receipt of the $82,500 was void as against any creditors whose debts arose after the date that the mortgage was recorded. *Id.* at 515. We held, however, that § 70e controlled, that the facts were similar to *Moore, i.e.*, the cases addressed chattel mortgages and § 70e claims, and stated that we were unable to distinguish *Moore* from that case. *Id.* at 515. We held therefore that the trustee was entitled to the $82,500, despite the invalidity of a creditor's claim against the Millers under California law. *Id.*

Many years later *in In re Acequia, Inc.*, 34 F.3d 800, 804 (9th Cir. 1994), we addressed whether a bankruptcy trustee's recovery for fraudulent transfers under § 544(b) (which replaced former § 70e) and § 550(a) could be limited to the amount of the unsecured claims against the bankrupt estate. In *Acequia*, Vernon Clinton formed Acequia, Inc. to conduct farming operations on his land in Idaho. *Id.* Later, Acequia filed for bankruptcy. *Id.* The

bankruptcy trustee for Acequia filed suit, asserting that Clinton had fraudulently conveyed Acequia's assets to himself and was liable under § 544(b) and § 550. *Id.* at 803-04, 808. Clinton argued that the § 544(b) claim was "moot because the corporation [had] paid all [of its] unsecured creditors in its plan of reorganization." *Id.* at 807.

In *Acequia*, we held that it was improper to limit a trustee's recovery under § 544(b) and § 550(a) based on the total amount of unsecured claims against the bankrupt estate. *Id.* We held that the existence of a § 544(b) claim requires only that one creditor exist at the time that the transfer was made and that that creditor have an actionable claim against the estate. *Id.* We held that a trustee must establish the following to recover under § 544(b) and § 550(a): 1) fraud or illegality under applicable law; 2) voidness of the transfer under § 544(b) and applicable law; and 3) liability of the particular transferee under § 550. *Id.* at 809. Once fraud and voidness are shown, a trustee may recover under § 550 to the extent it "benefits the estate," *i.e.*, even if there is a right to avoid a transfer, it does not mean that a right to recover on every transfer is automatic. *Id.* at 811.

Applying such rules in *Acequia*, we held that the bankruptcy trustee had a right to assert claims under § 544(b) because there were unsecured claims against the estate at the time that bankruptcy was filed. *Id.* at 807. We held that the trustee was entitled to fully recover, even if it received a windfall, because (1) recovery would ensure that Acequia would perform its obligations under its reorganization; (2) recovery would allow the estate to be reimbursed for pursuing the fraudulent transfer action; and (3) Clinton had

actual fraudulent intent and did not deserve between the two parties to receive a benefit. *Id.* at 811-12.

iii. Good Faith Transferee

[7] The trustee's position is that the interplay of §§ 544(b) and 550 requires full avoidance, and that California Civil Code § 3439.08(d)(3) is not applicable because Tramiel is not a good faith purchaser and § 3439.08(d)(3) cannot limit the transferee's avoidance. Both the bankruptcy court and the district court thought otherwise, as do we: § 3439.07, which allows relief of avoidance "to the extent necessary to satisfy the creditor's claim" is expressly made "subject to the limitations in Section 3439.08" — and those limitations include a reduction for what a good faith transferee paid.

While we held in *Miller* and *Acequia* that a trustee's recovery cannot be limited by certain factors when asserting a § 544(b) claim, those cases did not address the issue of good faith or this statutory provision, and we have held in other cases that certain factors — like good faith — apply as a matter of law when such a claim is raised. In *In re Agricultural Research and Technology Group, Inc.* ("*Agretech*"), 916 F.2d 528, 531 (9th Cir. 1990), we addressed whether the bankruptcy trustee for Agricultural Research and Technology Group, Inc. ("Agretech") could avoid fraudulent transfers made by Agretech to Palm Seedlings Partners-A ("Palm") under § 544(b) and § 550(a) and whether Palm was a good faith transferee under state law. *Id.* at 539. Agretech was a Hawaii corporation that took plant seeds, cultivated them and marketed the mature plants. *Id.* at 532. Several shipments of seeds were made to Agretech pursuant to

an agreement with Palm in which Agretech paid for the seeds and Palm agreed to pay a certain amount for the plants once they were grown. *Id.* at 533. Throughout its business dealings, however, Agretech was running a Ponzi scheme and distributing "funds to earlier investors from the receipt of monies from later investors." *Id.* at 536. Agretech's president plead guilty to operating a Ponzi scheme for several years, including years spanning the Palm agreement. *Id.* at 533.

We held that the transfers from Agretech to Palm were fraudulent and avoidable under § 544(b) and Hawaii Revised Statute § 651C-4(a)(1) and that Palm was not a good faith transferee under Hawaii Revised Statute § 651C-8. Under § 651C-4(a), a transfer is fraudulent as to a creditor if it was made with the intent to defraud or without receiving a reasonably equivalent value in exchange. Under § 651C-8, any transferee who received a transfer in good faith may recover the value he gave in a transaction which is avoidable under Hawaii Revised Statute § 651C-4(a)(1). *Id.* at 535. Because the record demonstrated that Agretech had actual intent to defraud its creditors by transferring the sums, we held that the transfers were avoidable under § 651C-4(a)(1). *Id.* at 538-39. We concluded that Palm did not constitute a good faith transferee under § 651C-8(a) because it should have known that Agretech was running a Ponzi scheme based on statements it made to Palm and from Agretech's willingness to accept little value in exchange for the transfer. *Id.* at 538-540. We held that this evidence showed Palm "not only knew of the fraud, but was an active participant." *Id.* at 539. Thus, Palm was not a good faith transferee.

In *In re AFI Holding, Inc.* ("*AFI*"), 525 F.3d 700, 701-02 (9th Cir. 2008), we addressed whether the trustee for Advance Finance Incorporated ("AFI") could avoid transfers from AFI to one of its investors, Keith Mackenzie, under § 548 and § 550 and whether Mackenzie was a good faith transferee under California Civil Code § 3439.08. *Id.* at 708-09. Mackenzie invested $73,400 with AFI in 1995 and 1996 as a purported limited partner in exchange for a proportionately reduced restitution claim. *Id.* at 702, 708. Mackenzie withdrew from AFI and received $89,824.18, which constituted his initial principal of $73,400 and a fictitious gain on his investment of $16,424. *Id.* at 702. Later, the founder of AFI pled guilty to federal securities and mail fraud charges and admitted to operating a Ponzi scheme. *Id.* at 704. The bankruptcy trustee sought to avoid the $89,824.18 transfer from AFI to Mackenzie and Mackenzie argued that he was a good faith transferee and entitled to a reduction on that basis. *Id.*

We held that the transfer from AFI to Mackenzie was an actual fraudulent transfer under § 548 and that the good faith transferee exception under California Civil Code § 3439.08 was not barred as a matter of law. *Id.* at 704-09. With regard to the fraud, we held that evidence of the Ponzi scheme and the guilty plea by AFI's founder sufficiently established actual intent to defraud creditors. *Id.* at 704. Regarding the good faith exception under § 3439.08, we stated that Mackenzie had exchanged a reasonably equivalent value for the transfer so that the good faith exception for the fraudulent transfer was not barred as a matter of law. *Id.* at 709. We held that if on remand the district court determined that Mackenzie took the transfer in good faith, then Mackenzie would be

entitled to the amount he gave AFI, *i.e.*, $73,400, but not to the fictitious gain of $16,424.18. *Id.* at 709.

[8] In this case, based on *Acequia, Agretech* and *AFI*, we hold that the trustee may recover under § 544(b) and § 550, but that Tramiel has shown he is a good faith transferee under California Civil Code § 3439.08. First, the trustee has established recovery under the three-part *Acequia* test. *Acequia*, 34 F.3d at 811. The *Acequia* test requires that the trustee show (1) fraud or illegality; (2) voidness of the transfer under § 544(b) and applicable law; and (3) liability of the particular transferee under § 550. *Id.* at 809. In this case, the trustee has satisfied steps one and two by showing that the real property transfer from JTS to Tramiel was a constructive fraudulent conveyance and was void under § 544(b) and California Civil Code § 3439.04(a). The trustee has also shown that Tramiel has liability for the transfer, but the amount of recovery must be calculated to the extent that it benefits the estate, as § 550 expressly requires, and must further the intent of § 550 to promote equity and restore the estate to its prior condition.

[9] To calculate the amount of recovery and abide by the intent of § 550, we hold that California Civil Code § 3439.08(d), the good faith transferee exception, applies in § 544(b) cases and, if satisfied, allows for a reduction in the trustee's recovery. Section 3439.08(d) provides that "[n]otwithstanding voidability of a transfer or an obligation under this chapter, a good faith transferee or obligee is entitled, to the extent of the value given the debtor for the transfer or obligation, to . . . [a] reduction in the amount of the liability on the judgment." Here, the record establishes that Tramiel was objectively a good faith transferee

who gave JTS $10 million in exchange for real property to enable JTS to survive financially. JTS had no source for capital and it was JTS who approached Tramiel and suggested that they do the real property transfer. To protect the company, Tramiel agreed to the deal, but gave JTS an option to repurchase the property at the exact same price for a period of a year. If JTS exercised the option, Tramiel would keep the greater of $1 million or the property's rental income and retain a return on his investment. Tramiel instructed board members that they should get an independent appraisal of the property and removed himself from all board discussions and votes regarding the transfer. Tramiel was not aware of any appraisals of the property and testified that he may have stated they were worth $12 to $13 million at the time of the merger. Finally, JTS board members stated that given the circumstances, and JTS's dire need for cash, the real property transaction was fair.

[10] In total, the evidence shows that Tramiel entered the transaction in good faith to enable the company to survive and proposed a repurchase option to protect the company. Because Tramiel is thus a good faith transferee under California Civil Code § 3439.08(d), his liability of $11,820,000 is reduced by any value that he gave in exchange for the real property. Tramiel gave $10 million to purchase the property and a repurchase option valued at $432,815, meaning that the total consideration provided for the property was $10,432,815. Deducting the amount of consideration, *i.e.* $10,432,815, from the amount of liability, *i.e.*, $11,820,000, leaves Tramiel with a liability of $1,387,185.

This conclusion effectuates the intent of § 550 to restore the bankrupt estate to the financial condition it enjoyed prior to the transfer. *Acequia*, 34 F.3d at 812. Allowing the estate to profit by taking value that should be returned to a good faith transferee does not promote the purpose of § 550 to restore equity. *Id.* Moreover, allowing state law good faith transferee exceptions in cases asserting § 544 claims permits a symmetry with the Bankruptcy Code: § 548 of the Bankruptcy Code, which voids fraudulent transfers under federal law, allows for a reduction in recovery due to a good faith transferee. Section 544(b), which allows for avoidance of fraudulent transfers under state law, should reflect this symmetry.

Thus, we hold that Tramiel is a good faith transferee under California Civil Code § 3439.08(d) and entitled to a reduction in liability of $10,432,815.

D. Settlement Credit

[11] Tramiel argues that he is entitled to a settlement credit pursuant to California Civil Procedure Code § 877 in the amount that his co-defendants paid to the estate to settle their claims, which was $4.5 million. Under § 877, where a covenant not to sue is given in good faith before a judgment "to one or more of a number of tortfeasors claimed to be liable for the same tort. . .it shall reduce the claims against the others in the amount stipulated by. . .the covenant, or in the amount of consideration paid for it whichever is greater." Section 877 allows joint tortfeasors to equitably share damages if they have committed the same tort. *Wakefield v. Bohlin*, 145 Cal. App. 4th 963, 979 (Cal. Ct. App. 2006), *overruled on other grounds by Goodman v. Lozano*, 47 Cal. 4th

1327, 1334 (2010); *May v. Miller*, 228 Cal. App. 3d 404, 407 (Cal. Ct. App. 1991). Its fundamental purpose "is to preclude a double recovery arising out of the same wrong." *Vesey v. United States*, 626 F.2d 627, 633 (9th Cir. 1980).

i. Same Injury

[12] Whether individuals are joint tortfeasors under § 877 depends upon whether they caused "one indivisible injury" or "the same wrong." *May*, 228 Cal. App. 3d at 409-10; *Lafayette v. County of Los Angeles*, 162 Cal. App. 3d 547, 554 (Cal. Ct. App. 1984). The "same wrong" may emanate from two successive independent torts and does not require unity of purpose, action, or intent by the two or more tortfeasors. *Id.* at 554; *Kohn v. Superior Court of San Mateo*, 142 Cal. App. 3d 323, 328 (Cal. Ct. App. 1983). Also, the plaintiff need not allege the same tort against the tortfeasors, but must only claim that the tortfeasors caused the same harm. *Lafayette*, 162 Cal. App. 3d at 555-56.

In *Lafayette v. County of Los Angeles*, 162 Cal. App. 3d 547 (1984), for example, plaintiff sued the county for medical malpractice and his attorney for legal malpractice in the handling of his medical malpractice action. *Id.* at 550, 553. The attorney settled before trial and paid plaintiff $15,000. *Id.* at 554. At trial, the jury found that the county was liable in the amount of $84,000. *Id.* at 550. The court held that plaintiff's injury by the county and his attorney were the "same wrong" and allowed a reduction by the $15,000 settlement paid to plaintiff by his attorney under § 877. *Id.* at 555. The court stated that "two tortfeasors can both be liable for the same tort without being joint

tortfeasors in the sense of concert of action and unity of purpose." *Id.* at 554. The court explained that

> In *Helling v. Lew* (1972) 28 Cal. App. 3d 434, 104 Cal. Rptr. 789, tortfeasor 1 caused injury to plaintiff who was required to seek medical care from tortfeasor 2 who malpracticed the plaintiff. The plaintiff, of course would be entitled under recognized principles of proximate causation to recover against tortfeasor 1 for the damages caused by tortfeasor 2. Therefore, an offset was allowed to tortfeasor 1 for a settlement made with tortfeasor 2. Specifically, tortfeasor 1 and tortfeasor 2 were both liable for damages from the second tort-medical malpractice. To avoid double recovery, tortfeasor 1 was entitled to an offset for the settlement with tortfeasor 2.

Id. at 555 (internal quotation marks omitted). The court also stated that it is not necessary that plaintiff allege the same tort against the joint tortfeasors. *Id.* at 555-56. The court held that § 877 applies if the plaintiff claimed that the tortfeasors were liable for the same wrong and here plaintiff "clearly claimed Rose was liable for the damages resulting from the County's tort." *Id.* at 556.

Similarly, in *Knox v. County of Los Angeles*, 109 Cal. App. 3d 825 (Cal. Ct. App. 1980), plaintiffs who claimed that they were unlawfully arrested in front of a market while picketing it sued the market and the county for damages. *Id.* at 828-29. Plaintiffs alleged they were arrested at the instigation and direction of the market defendants which then proximately caused the unlawful arrests and false imprisonment. *Id.* at 829. Prior to trial, plaintiffs settled with the market

for $4,000 per plaintiff. *Id.* at 830-31. At trial, the jury found that the county was liable for $17,500 damages to each plaintiff. *Id.* The court held that the county was entitled to a setoff of $4,000 per plaintiff under § 877 because both parties were claimed to have been liable for the unlawful arrests and false imprisonment. *Id.* at 831-32.

In *Kohn v. Superior Court of San Mateo*, 142 Cal. App. 3d 323, 328 (Cal. Ct. App. 1983), the plaintiffs sued a pest control company, construction company, and the sellers of a house for negligence and fraud. Plaintiffs bought a house for $60,500 and the sellers failed to disclose that the home had been involved in a fire. *Id.* at 325. The construction company defendant repaired the fire damage to the home and the pest control company conducted an inspection while the house was in escrow. *Id.* at 325. Prior to trial, the pest control company and construction company settled with plaintiff with each defendant paying $6,000. *Id.* at 325. Plaintiffs sought $500,00 from the remaining seller defendants who attacked the validity of the settlement agreement because it was a markedly low amount. *Id.*

The court held that the settlement agreement was valid and that § 877 applied. *Id.* at 328-30. The court held that the "alleged tortious activities by the contractor, pest control inspector and seller were not independent, but combined to create one indivisible injury which took place when the sale [of the house] was consummated." *Id.* at 329. The court also held that although plaintiff alleged that the settling defendants were liable for failure to inspect and repair properly, and alleged that the nonsettling sellers were liable for fraud, that did not alter the outcome since there was

but one injury, *i.e.*, the purchase of a home which was worth less than its value. *Id.* at 328-29.

In this case, the bankruptcy court properly determined that Tramiel and the settling co-defendants committed the "same injury" pursuant to § 877. The trustee asserted in her complaint that Tramiel was liable for breach of fiduciary duty based on the real property transfer and constructive fraudulent conveyance based on the real property transfer. The trustee asserted that the settling attorney defendants were liable for *inter alia* breach of fiduciary duty and aiding and abetting in breach of fiduciary duty related to the real property transfer. The trustee asserted that the settling director defendants were liable for knowingly approving the real property transfer despite knowledge that it was fraudulent. In the complaint, the trustee alleged that all defendants were jointly liable for the concerted and separate acts which culminated in the real property transfer to Tramiel and that they knew of the disparity between the purchase price and fair market value of the real property.

[13] Here, the trustee alleged Tramiel and the settling defendants combined to carry out the same injury, *i.e.*, the fraudulent transfer of the real property. The settling attorneys, other directors, and Tramiel all acted to further the transaction which is the harm that the trustee alleges. It is irrelevant that the trustee alleged different torts against Tramiel and the settling defendants since their concerted conduct produced the same injury and the decision to sell the property by the settling directors with the aid of the attorneys proximately caused the actual harm of the real property transaction. *See Knox*, 109 Cal. App. 3d at

832-33; *Kohn*, 142 Cal. App. 3d at 329; *Lafayette*, 162 Cal. App. 3d at 555-56. Thus, the bankruptcy court properly found that § 877 was applicable in this case because the separate conduct of Tramiel and the settling defendants combined to create the same indivisible injury, which was the sale of the real property at less than its value.

ii. Amount of Offset

[14] Under § 877, the amount of plaintiff's recovery is " 'diminished only by the amount plaintiff actually recovered in a good faith settlement rather than by an amount measured by the settling tortfeasor's proportionate responsibility for the injury.' " *Knox*, 109 Cal. App. 3d at 834 (quoting *McGee v. Cessna Aircraft Co.*, 82 Cal. App. 3d 1005, 1022 (1978)). In *Alcal Roofing & Insulation v. Superior Court of San Mateo*, 8 Cal. App. 4th 1121, 1123 (Cal. Ct. App. 1992), a condominium association asserted a construction defect case against the developer, roofing-related subcontractors, and a roofer. All parties agreed to a settlement amount of $4.4 million, except the roofer. In the settlement agreement, the parties allocated $100,000 for roofing claims. The roofer argued that the court should not have approved the settlement because this was far less than his possible liability and would lessen the amount of offset applicable to any judgment against him. The court held that if each settling defendant allocated its settlement to primarily nonroofing issues the roofer could "obtain an offset for the settlement of each of the other defendants, limited only by the amount of each settlement." *Id.* at 1127.

Similarly, in *L.C. Rudd & Son, Inc. v. Superior Court of Alameda*, 52 Cal. App. 4th 742 (Cal. Ct. App.

1997), a homeowners association brought a construction defects case against various developers, a contractor, and a rough grader. There, the developers agreed to "settle with plaintiff for a total cash consideration of $90,000 plus assignment of developers' indemnity rights against the nonsettling parties." *Id.* at 745. The nonsettling defendant, the contractor, brought suit arguing that the agreement was not in good faith. The court held that where "parties to a lawsuit settle 'in good faith before verdict or judgment' the settling tortfeasor is released from all liability for any contribution to any other tortfeasors and the claims against the nonsettling tortfeasors will be reduced by the amount of the contribution paid for the release of the settling tortfeasor." *Id.* at 747. The court stated that § 877 favors settlement and that to preserve the incentive to settle, " 'a plaintiff's recovery from nonsettling tortfeasors should be diminished only by the amount that the plaintiff has actually recovered in a good faith settlement, rather than by an amount measured by the settling tortfeasor's proportionate responsibility for the injury.' " *Id.* at 751 (quoting *Am. Motorcycle Ass'n v. Superior Court*, 20 Cal. 3d 578, 604 (Cal. 1978)). The court held that the plaintiff was entitled to an offset of the entire amount of the settlement and not just an amount attributable to his liability. *Id.* at 752.

[15] In this case, the settlings defendants agreed to settle with the trustee for the amount of $4.5 million. In the settlement agreement, the attorney defendants agreed to pay $3,075,000 and the directors agreed to pay $825,000 and $600,000. The agreement also provided that the trustee allocate the $3,075,000 to malpractice claims, and the directors' payments to forgiveness of promissory notes and repurchase of

shares. In approving the settlement, the bankruptcy court reserved the right to find Tramiel a joint tortfeasor, which it did orally, and it found no stipulated good faith allocation given that the agreement merely recites that the trustee assigned the settlement to the non-joint claims. Although the settlement agreement does not allocate an amount of liability for Tramiel's harm, based on *Alcal*, Tramiel is entitled to an offset under § 877 of the entire settlement amount paid to the trustee. Thus, Tramiel is entitled to a settlement credit of $4.5 million. 8 Cal. App. 4th at 1127-28.

E. Director Preferences

[16] Decker argues that the repayment of a $3 million loan plus interest in the amount of $40,201 to the Amber Group, consisting of several directors including Tramiel, was a per se illegal director preference under Delaware law. *See Pennsylvania Co. for Insurances on Lives & Granting Annuities v. South Broad St. Theatre Co.*, 174 A. 112, 116 (Del. Ch. 1934) (indicating impossibility of reconciling conduct of stockholders of a failing corporation who favor themselves as against creditors with honesty and good faith). However, *Penn. Co.* did not adopt a per se rule, and we believe there are special circumstances in this case that tip in favor of Tramiel as a director-creditor. Amber Group made the $3 million loan for a purpose not motivated by self-interest — to help JTS maintain operations while it negotiated a sale of intellectual property. The loan was secured by this intellectual property. When JTS sold the property of $5 million, it paid off the $3 million, while leaving JTS with $2 million more in revenue than it would have had — and

with the purpose of the loan fulfilled. As a result, this was not an unlawful director preference.

Conclusion

[17] Accordingly, we hold that Tramiel's liability for the constructive fraudulent conveyance is $11.8 million, that this amount is reduced by $10,432,815 million because Tramiel is a good faith transferee under California Civil Procedure Code § 3439.08, and that Tramiel is entitled to a settlement credit of $4.5 million under California Civil Code § 877. Thus, Tramiel has no liability to the trustee for the conveyance.

AFFIRMED.

APPENDIX B

NOT FOR CITATION

IN THE UNITED STATES DISTRICT COURT FOR THE NORTHERN DISTRICT OF CALIFORNIA SAN JOSE DIVISION

Case Number C 05-4709 JF

[Filed May 4, 2007]

IN RE JTS CORPORATION, a Delaware corporation, fka ATARI CORPORATION, Debtor.	)
SUZANNE L. DECKER, Trustee, Appellant-Plaintiff, v. JACK TRAMIEL, Appellee-Defendant.	)

ORDER DENYING CROSS-MOTIONS FOR RECONSIDERATION

Appellant-Plaintiff Suzanne L. Decker, the chapter 7 bankruptcy trustee ("the Trustee"), and Appellee-Defendant Jack Tramiel ("Tramiel") have filed cross-motions for reconsideration of this Court's disposition of the Trustee's appeal of the bankruptcy court's judgment in her adversary proceeding against directors, attorneys and shareholders of the debtor company, JTS Corporation ("JTS"). The Court, having considered the briefing of the parties as well as the oral arguments presented at the hearing on December 15, 2006, resolves the cross-motions for reconsideration as follows:

I. DISCUSSION

(A) Procedural Issue

The Trustee characterizes her motion as a motion for rehearing under Federal Rule of Bankruptcy Procedure 8015, which is the proper vehicle for the motion. Tramiel characterizes his motion as a motion to amend judgment under Federal Rule of Civil Procedure 59(e) or as a motion for relief from judgment under Federal Rule of Civil Procedure 60(b). The Trustee asserts that Tramiel's motion under these rules is procedurally improper, and that any such motion must be brought under Federal Rule of Bankruptcy Procedure 8015. The Court concludes that the Trustee is correct. However, because the Trustee has not suffered any prejudice from Tramiel's mischaracterization of his motion, the Court construes Tramiel's motions as being brought under Federal Rule of Bankruptcy Procedure 8015.

B. Trustee's Motion

1. Interplay Between Bankruptcy Code And California Fraudulent Transfer Law

In its order addressing the Trustee's appeal issued September 29, 2006, this Court devoted significant time and analysis to the interplay between the Bankruptcy Code and California's fraudulent transfer laws, and ultimately concluded that the limit on liability for a good faith purchase imposed by California Civil Code § 3439.08(d) (the provision allowing a good faith purchaser to set off monies paid in the transaction) was imported into 11 U.S.C. § 544(b) and 550(a) along with other provisions of California's fraudulent transfer laws. The Trustee argues that the Court is simply wrong in its analysis, citing various Supreme Court and Ninth Circuit cases that she asserts establish the general rule that a transfer that is only partially avoidable under state law is fully avoidable under bankruptcy law. These cases include *Moore v. Bay*, 52 S.Ct. 3 (1931) and *Miller v. Sulmeyer*, 263 F.2d 513 (9th Cir. 1959). These cases do not address the particular California statutes at issue. They were cited by the Trustee in the original briefing, although they were not explicitly addressed in the Court's order on the appeal. The Court has revisited the cases cited by the Trustee, but is not inclined to change its legal conclusion regarding the applicability of California Civil Code § 3439.08(d) on the facts of this case. Accordingly, this portion of the Trustee's motion for reconsideration will be denied.

The Trustee also attacks once again the conclusion that Tramiel was a good faith transferee. Tramiel's good faith was a factual finding by the bankruptcy

court that this Court concluded was not clearly erroneous. The Trustee has not presented a sufficient basis for reconsideration of this conclusion.

2. Debt Relief

This Court upheld the bankruptcy court's factual finding that the debt relief was not a purchase or redemption of shares, and thus did not fall within 8 Del. C. § 160, prohibiting a corporation from purchasing or redeeming its own shares when the capital of the corporation is impaired. The Trustee argues that regardless of what the corporation *called* the transaction, the fact is that the corporation impaired its capital by releasing Tandon from a $1 million promissory note and thereby reacquired stock. The Court concludes that the cases cited by the Trustee cannot be read as broadly as argued by the Trustee. The Court therefore declines to reconsider its conclusion that the bankruptcy court did not clearly err with respect to its characterization of the debt relief to Tandon and Mitchell.

C. Tramiel's Motion

(1) Value Of The Option

The bankruptcy court valued the repurchase option in the real estate transaction at $432,815. Tramiel did not challenge this value on appeal. The Court thus adopted this value of the option in calculating Tramiel's set off for value paid under California Civil Code § 3439.08(d). Tramiel now argues that $432,815 is not the appropriate value of the option.

When the bankruptcy court calculated Tramiel's set off and liability for the real estate transaction, the court subtracted the value Tramiel paid from the properties' *reasonably equivalent value*, finding that the difference between what Tramiel paid and the properties' fair value was $1,387,185. The bankruptcy court thus found that the transaction could be avoided in the amount of $1,387,185. This Court concluded that the proper calculation was to subtract the value that Tramiel paid from the properties' *fair market value*, and found that difference to be $6,714,370. Tramiel argues that the proper calculation for the value of the option is to subtract the strike price from the fair market value, citing *In re Calvillo*, 263 B.R. 214 (W.D. Tex. 2000). Tramiel argues that the bankruptcy court assigned fair market value of $11,820,000 and then subtracted the strike price of $11,387,185 to obtain the option value of $432,815. Tramiel argues that if this Court is going to change the fair market value to $17,147,000, then the value of the option must go up, because the formula stays the same. Tramiel argues that if the strike price of $11,387,185 is subtracted from the fair market value of $17,147,000, the result is an option value of $5,759,815. If Tramiel is allowed to set off the $10 million he paid, plus the $5,759,815 value of the option he gave in the transaction, his total liability is $1,387,185, the number arrived at by the bankruptcy court.

Tramiel's arguments are unpersuasive because (1) he did not appeal the bankruptcy court's option valuation and (2) the bankruptcy court stated explicitly that it was *not* using the *Calvillo* formula and in fact did not use that formula. While the bankruptcy court erroneously referred to the

$11,820,000 as the fair market value at times, it is clear from the bankruptcy court's decision as a whole that it actually characterized this figure as the reasonably equivalent value, which was fair market value discounted for bundling and quick sale. Accordingly, this Court concludes that Tramiel has not presented any basis to recalculate the option value.

2. Settlement Credit

Tramiel objects to the Court's determination that the evidence demonstrated that the $4.5 million in settlement proceeds were allocated to claims other than the claim for which Tramiel was found liable, and thus that Tramiel is not entitled to a credit for any part of that settlement. Tramiel essentially rehashes his arguments presented in the context of the appeal. The Court addressed these arguments in its order on the appeal.

Tramiel also argues that aside from the settlement proceeds of $4.5 million previously addressed by this Court, there were additional settlement proceeds of $4 million, and that he is entitled to a credit for the $4 million amount. Tramiel did not raise this issue on appeal. He argues that the bankruptcy court never addressed the question of whether he was entitled to a credit for the remaining $4 million in settlement proceeds, because the bankruptcy court determined that he was entitled to a credit for the $4.5 million, and that was enough to wipe out his liability. He suggests remand to the bankruptcy court for determination as to the earlier settlement proceeds. However, as the Trustee points out, Tramiel easily could have cross-appealed with respect to the remaining $4 million once the Trustee made clear its

position that Tramiel was not entitled to a credit for the $4.5 million. Accordingly, the Court declines to reconsider its ruling on the settlement credit or to remand for further proceedings on this point.

II. ORDER

The parties' cross-motions for reconsideration are DENIED.

DATED: 5/4/07

/s/ Jeremy Fogel
JEREMY FOGEL
United States District Judge

[*Certificate of Service omitted in printing*]

* * *

APPENDIX C

NOT FOR CITATION

IN THE UNITED STATES DISTRICT COURT FOR THE NORTHERN DISTRICT OF CALIFORNIA SAN JOSE DIVISION

Case Number C 05-4709 JF

[Filed September 29, 2006]

IN RE	)
	)
JTS CORPORATION, a Delaware corporation, fka ATARI CORPORATION,	)
	)
Debtor.	)
	)
SUZANNE L. DECKER, Trustee,	)
	)
Appellant-Plaintiff,	)
	)
v.	)
	)
JACK TRAMIEL,	)
	)
Appellee-Defendant.	)
	)

ORDER RE TRUSTEE'S APPEAL

Appellant-Plaintiff Suzanne L. Decker, the chapter 7 bankruptcy trustee ("the Trustee") appeals the bankruptcy court's judgment in her adversary proceeding against directors, attorneys and shareholders of the debtor company, JTS Corporation ("JTS"). The Court, having considered the briefing of the parties as well as the oral arguments presented at the hearing on September 8, 2006, resolves the appeal as follows:

I. BACKGROUND

JTS was formed in 1994 to design, manufacture and market a smaller, slimmer hard disk drive to be used in personal computers. JTS suffered serious financial setbacks in 1996 when it lost a major contract with Compaq. JTS then merged with Atari Corporation ("Atari") in order to obtain much-needed funds. Atari's chairman of the board, Jack Tramiel ("Tramiel"), became a member of JTS's board of directors following the merger. Among the other directors on JTS's board at that time were its chairman, Jugi Tandon ("Tandon"), and its president and chief executive officer, David Mitchell ("Mitchell").

Following the merger, JTS liquidated real and intellectual property in an effort to generate sufficient cash to stay afloat. However, by July 1997 the disk drive market was glutted. JTS abandoned production of a smaller disk drive and pursued a new business model based on a very low-cost, high capacity disk drive. These efforts were unavailing. JTS was forced into bankruptcy through involuntary petition in November 1998 and subsequently filed a voluntary

petition for relief under chapter 11, scheduling assets of $4.2 million and liabilities of $136 million. The case converted to chapter 7 in January 1999.

The Trustee filed an adversary proceeding against JTS's directors and attorneys as well as a major shareholder, alleging claims of breach of fiduciary duty, preference, fraudulent conveyance, equitable subordination, avoidance of transfers, illegal redemption of shares, legal malpractice, alter ego liability, unfair business practices, aiding and abetting and conspiracy.

The bankruptcy court adjudicated certain aspects of the Trustee's claims in an order addressing the parties' cross-motions for summary judgment issued September 30, 2003 ("Summary Judgment Order"). Subsequently, Tandon, Mitchell and the attorney defendants reached settlement with the Trustee, under which the settling defendants paid the estate $4.5 million. On April 23, 2005, the bankruptcy court issued an order approving good faith settlement.

The adversary proceeding went to trial against only one defendant, Tramiel. The bankruptcy court issued an opinion following trial on September 30, 2005 and entered judgment on October 31, 2005. The judgment stated that Tramiel was liable in the amount of $1,387,185 plus prejudgment interest and explicitly stated that Tramiel was not entitled to a settlement credit for the prior $4.5 million settlement of his co-defendants. Tramiel filed a motion to amend the judgment to permit him a settlement credit. That motion was heard on December 22, 2005 and was granted on the same date. An amended judgment was entered on January 19, 2006 providing that Tramiel

may apply a settlement credit in the amount of $4.5 against his liability. This amendment to the judgment in effect reduced Tramiel's liability to zero, because the $4.5 settlement credit exceeded the amount for which he had been adjudicated liable.

II. LEGAL STANDARD

A bankruptcy court's factual findings are reviewed for clear error and its legal conclusions are reviewed *de novo*. *In re Strand*, 375 F.3d 854, 857 (9th Cir. 2004). A bankruptcy court's grant of summary judgment is reviewed *de novo*. *In re Lee*, 335 B.R. 130, 135 (BAP 9th Cir. 2005).

III. DISCUSSION

The Trustee's appeal focuses on three transactions addressed by the bankruptcy court, addressed in turn as follows:

A. The Real Estate Transaction

The 1996 merger with Atari did not solve JTS's cash problems. In mid-1996, JTS's chief financial officer approached Tramiel about purchasing a portfolio of eight real properties that JTS had acquired from Atari as part of the merger. Tramiel agreed to purchase the entire portfolio of properties for total book value of $10 million, with JTS retaining an option to repurchase for $10 million within the first year. If JTS exercised the option, Tramiel would keep the greater of $1 million or the rental income generated by the properties during the one-year option period. The option expired without being exercised. Tramiel

subsequently transferred the real property portfolio to an entity for the benefit of his children.

The Trustee asserted that the sale of the real properties to Tramiel was avoidable as a constructive fraudulent conveyance under 11 U.S.C. § 544(b), which provides that a trustee "may avoid any transfer of an interest of the debtor in property or any obligation incurred by the debtor that is voidable under applicable law by a creditor holding an unsecured claim . . . ." "[T]o the extent that a transfer is avoided under section 544 . . . the trustee may recover, for the benefit of the estate, the property transferred, or, if the court so orders, the value of such property." 11 U.S.C. § 550(a). "In seeking recovery of such monies, the trustee stands in the overshoes of the debtor corporation's unsecured creditors." *In re Agricultural Research & Tech. Group, Inc.*, 916 F.2d 528, 534 (9th Cir. 1990).

The Trustee invoked § 544(b) to apply California's fraudulent conveyance laws. Specifically, the Trustee looked to California Civil Code § 3439.04(a), which provides *inter alia* that a transfer is fraudulent if made by a debtor who did not receive "reasonably equivalent value" and either (a) the debtor was engaged or was about to engage in business for which the debtor's remaining assets were unreasonably small in relation to the business or (b) the debtor intended to incur or should have believed that he would incur debts beyond his ability to pay as they became due. Cal. Civ. Code § 3439.04(a). California Civil Code § 3439.07 sets forth the remedies for a fraudulent transfer, providing that, "subject to the limitations in Section 3439.08," a creditor may obtain "[a]voidance of the transfer or obligation to the extent necessary to

satisfy the creditor's claim." Cal. Civ. Code § 3439.07(a). The limiting provision, California Civil Code § 3439.08, provides that to the extent a transfer is voidable under § 3439.07, a creditor "may recover judgment for the value of the asset transferred, as adjusted under subdivision (c), or the amount necessary to satisfy the creditor's claim, whichever is less." Cal. Civ. Code § 3439.08(b). Subdivision (c) provides that judgment shall be equal to the value of the asset at the time of the transfer, "subject to adjustment as the equities may require." Cal. Civ. Code § 3439.08(c). Subdivision (d) provides an additional limitation, stating that "[n]otwithstanding voidability of a transfer or an obligation under this chapter, a good faith transferee or obligee is entitled, to the extent of the value given the debtor for the transfer or obligation, to ... [a] reduction in the amount of the liability on the judgment." Cal. Civ. Code § 3439.08(d)(3).

Applying California Civil Code § 3439.04, the bankruptcy court found that JTS did not receive "reasonably equivalent value" for the properties and that JTS was insolvent at the time of the transaction. The bankruptcy court's finding of insolvency appears to be a kind of shorthand for satisfaction of the requirement that (a) the debtor was engaged or was about to engage in business for which the debtor's remaining assets were unreasonably small in relation to the business or (b) the debtor intended to incur or should have believed that he would incur debts beyond his ability to pay as they became due. *See* Cal. Civ. Code § 3439.04(a)(2). Satisfaction of these elements is not at issue in this appeal.

With respect to the requirement that the debtor did not receive "reasonably equivalent value," the bankruptcy court concluded that the eight properties had an aggregate fair market value of $15,760,000 at the time of the sale. However, for purposes of determining "reasonably equivalent value," the court discounted the fair market value 20% because the properties were bundled and discounted an additional 5% for the quick sale. The court thus concluded that for purposes of determining "reasonably equivalent value" at the time of sale the properties fairly could be valued at $11,820,000. The court further concluded that the value JTS received in exchange for the properties was the $10 million in cash plus the value of the repurchase option, which the court put at $432,815. Based on these valuations, the court found that JTS received $1,387,185 less than the value of the properties sold, and thus did not receive "reasonably equivalent value." Accordingly the court concluded the transfer was fraudulent under California Civil Code § 3439.04.

The court concluded further that the Trustee could avoid the transaction pursuant to California Civil Code § 3439.07(a)(1). However, it found that Tramiel had acted in good faith in purchasing the property, and therefore that under California Civil Code § 3439.08(d), Tramiel was entitled to a reduction of his liability by the amount he had paid JTS. The court thus concluded that the transfer was avoidable in the amount of $1,387,185 – the fair value of the property at the time of transfer less the value that Tramiel paid.

Finally, the bankruptcy court concluded that Tramiel was entitled to a credit for the $4.5 million

settlement entered into by his co-defendants. Because the credit was greater than Tramiel's liability, the bankruptcy court concluded that Tramiel's net liability was zero.

The Trustee asserts that the bankruptcy court's calculation of Tramiel's liability was erroneous. Specifically, the Trustee asserts that *once the avoidability* of the transfer is determined pursuant to state law, the *amount* of Tramiel's liability should be determined pursuant to 11 U.S.C. § 550(a), which the Trustee asserts imposes liability in the amount of the full market value of the property transferred and does not make any provision for reduction for consideration paid. In short, the Trustee asserts that the proper approach is to determine whether the transfer was fraudulent under California Civil Code § 3439.04, but to omit the specific limitation on liability for such fraudulent transfer – i.e., reduction in liability in the amount of value given the debtor – imposed by California Civil Code § 3439.08(d).

(1) Interplay Between Bankruptcy Code And California Fraudulent Transfer Law

This appears to be a novel issue of law. As noted above, the bankruptcy court's legal conclusions are subject to *de novo* review. The parties have not cited, and the Court has not discovered, any cases expressly addressing the interplay between 11 U.S.C. §§ 544(b) and 550(a) on the one hand, and California Civil Code § 3439.08(d) on the other hand. The Trustee relies heavily upon the Ninth Circuit's decision in *In re Acequia, Inc.* for the proposition that once a transfer is identified as fraudulent under state law, the extent of

the recovery is governed solely by 11 U.S.C. § 550(a). *Acequia* is not precisely on point, however. In that case, the debtor-in-possession, Acequia, invoked 11 U.S.C. § 544(b) to apply Idaho's fraudulent conveyance laws, specifically a provision deeming fraudulent any conveyance made with actual intent to defraud. The magistrate judge concluded that the transfer in question was fraudulent under this provision but, reasoning that Acequia's rights under § 544(b) derived from those of its unsecured creditors, limited Acequia's recovery to the total amount of unsecured claims against the bankruptcy estate. The Ninth Circuit held that this limitation was erroneous, stating that once a trustee has established the *right* to avoid a transfer under 11 U.S.C. § 544(b) – that is, under applicable state law – the *amount* of such recovery is governed by 11 U.S.C. § 550(a). *In re Acequia*, 34 F.3d 800, 809 (9th Cir. 1994). Consequently, if a trustee establishes that a particular transfer is avoidable under state law because it is fraudulent as to a particular creditor, the transfer may be *entirely* avoided regardless of the size of the creditor's claim. *Id.* at 809-10. The extent of the trustee's recovery is governed by 11 U.S.C. § 550(a), which requires only that recovery be for "the benefit of the estate."

The rule of *Acequia* may be summarized as follows: a trustee may avoid a fraudulent transfer to the full extent permitted under applicable state law, even if such avoidance exceeds the amount of the unsecured creditors' claims, if such avoidance is for "the benefit of the estate." The bankruptcy court that adjudicated Tramiel's liability in this case applied this very rule in *In re Serrato*. In that case, the bankruptcy court addressed language in California Civil Code § 3439.07 limiting a creditor's recovery for fraudulent transfer to

the amount necessary to satisfy the creditor's claim. The Court held that this express state statutory limitation on a creditor's right to recover for fraudulent conveyance did *not* limit a trustee's right to recover under 11 U.S.C. §§ 544(b) and 550(a), citing *Acequia* for the proposition that "[t]he Bankruptcy Code separates 'the concepts of avoiding a transfer and recovering from the transferee.'" *In re Serrato*, 214 B.R. 219, 231 (1997) (quoting *Acequia*, 34 F.3d at 808). The bankruptcy court also cited *Acequia* for the proposition that "[a]lthough the trustee has demonstrated her right to recovery under state law, she must still establish the amount of recovery pursuant to § 550(a) of the Bankruptcy Code." *Id.*

The question before this Court is whether the limit on liability imposed by California Civil Code § 3439.08(d), expressly reducing a California creditor's recovery for fraudulent transfer, should be disregarded in a similar manner on the ground that the amount of recovery for a fraudulent transfer is governed solely by 11 U.S.C. § 550(a). As noted above, there do not appear to be any published opinions squarely addressing this precise issue. However, two published decisions clearly assume – albeit without discussion – that similar setoff provisions in other states' fraudulent conveyance laws apply when those laws are invoked via 11 U.S.C. § 544(b). In *In re Agricultural Research & Tech. Group, Inc.*, the Ninth Circuit noted that under the applicable Hawaii fraudulent transfer law, a good faith transferee is entitled to recover any value given in the transaction. *Agricultural Research*, 916 F.2d at 539. The court ultimately determined that the transferee had failed to demonstrate good faith, but it is clear from the decision that had the transferee made a showing of good faith the court would have concluded

that the transferee was entitled to a setoff for value given in the transaction.

The *Agricultural Research* decision predates *Acequia*. However, a published bankruptcy court decision rendered several years after *Acequia* reaches the same result. In *In re Viscount Air Services, Inc.*, the trustee invoked § 544(b) to apply Arizona's fraudulent conveyance law. *In re Viscount Air Services, Inc.*, 232 B.R. 416, 432 (Bankr. D. Ariz. 1998). Under Arizona law, a transferee who takes in "good faith" is entitled to set off the amounts paid for the transfer. *Id.* at 440. The bankruptcy court found that the transferee acted in good faith and thus was entitled to a setoff to the extent of monies paid for the transfer, and that to rule otherwise would unfairly penalize the transferee. *Id.* The bankruptcy court did not expressly consider the impact of *Acequia* and its progeny in reaching this decision.

Because these decisions do not squarely address the relevant issue, their persuasive authority is quite limited. However, the decisions do demonstrate that at least two courts have assumed that state law setoff provisions like the one at issue here are swept into 11 U.S.C. § 544(b) along with provisions defining a fraudulent conveyance. Moreover, although the Trustee correctly points out that California Civil Code § 3439.08(d) properly is characterized as a limit on *liability* rather than a limit on *avoidability*, the statutory provision authorizing avoidance states expressly that a creditor may obtain avoidance "subject to the limitations in Section 3439.08." Accordingly, while acknowledging that the appropriate interplay of the Bankruptcy Code and California's fraudulent conveyance law is far from clear in the present context,

the Court concludes that the bankruptcy court properly permitted Tramiel to set off the value he gave for the properties when adjudicating his liability.

(2) Whether Tramiel Acted In Good Faith

The Trustee argues that even if the good faith setoff provided in California Civil Code § 3439.08(d) applies, the bankruptcy court erred in finding that Tramiel acted in good faith. The bankruptcy court's factual finding of good faith is reviewed for clear error. After reviewing the record, as well as the bankruptcy court's careful reasoning on this point, this Court has no difficulty concluding that the bankruptcy court's finding of good faith was not clearly erroneous.

(3) Proper Methodology For Calculating Tramiel's Liability

This Court agrees with the Trustee that the bankruptcy court erred when it calculated Tramiel's liability. Assuming without deciding that the bankruptcy court's discounting of the properties' fair market value was appropriate for the purpose of determining whether JTS received "reasonably equivalent value," the Court is not persuaded that "reasonably equivalent value" is the appropriate measure of Tramiel's liability.

The Bankruptcy Code provides that the trustee may recover "the property transferred" or alternatively "the value of such property." 11 U.S.C. § 550(a). The statute does not define "value." However, the majority of cases addressing the issue have held that fair market value is the appropriate starting point for determining liability in a fraudulent transfer case. *See,*

e.g., *In re Kemmer*, 265 B.R. 224, 236 (Bankr. E.D. Cal. 2001) (holding that appropriate measure of liability under 11 U.S.C. § 550(a) was the value of the equity transferred, that is, the fair market value of the property less its encumbrances); *In re Walter*, 261 B.R. 139, 145 (Bankr. W.D. Pa. 2001) (holding that appropriate measure of liability under 11 U.S.C. § 550(a) is fair market value of transferred property); *In re Vann*, 26 B.R. 148, 149 (Bankr. S.D. Ohio 1983) (using fair market value as measure of liability under 11 U.S.C. § 550(a)); *Matter of Nevada Implement Co.*, 22 B.R. 105, 107 (Bankr. W.D. Mo.1982) (stating that fair market value is appropriate measure of liability under 11 U.S.C. § 550(a)). The Court thus concludes that the appropriate measure of liability is the fair market value of what Tramiel acquired – the properties and the rents – less any value he gave JTS. The bankruptcy court found that the experts had established the fair market value of the properties to be $15,760,000 and the fair market value of the rents to be $1,387,185, for a total fair market value of $17,147,185. Tramiel gave JTS $10 million in cash plus an option to repurchase that the bankruptcy court valued at $432,815, for total value given by Tramiel of $10,432.815. Tramiel's liability thus is $17,147,185 with a setoff of $10,432,815, or $6,714,370.

(4) Availability Of Settlement Credit

Approximately one year before the adversary action went to trial against Tramiel, the bankruptcy court approved a settlement agreement between the Trustee, Tandon, Mitchell and the attorney defendants. The settlement agreement provided that the settling defendants would pay the Trustee a total of $4.5 million. Settlement Agreement ¶ 1.1. The settlement

agreement explicitly allocated the $4.5 million to particular claims, as follows:

> The Settlement Sum shall be paid as follows: (1) The Attorney Defendants shall pay $3,075,000 which the Trustee allocates to the claims of malpractice related to Series B and C and forgiveness of indebtedness. . . . (2) Mitchell shall pay $600,000 and Tandon shall pay $825,000, which payments the Trustee allocates to the claims related to the forgiveness of promissory notes and the repurchase of those shares with those notes.

Id. The settlement agreement contains an integration clause providing that the settlement agreement contains the full expression of the parties' agreement. *Id.* at ¶ 16. All of the settling defendants signed the settlement agreement.

Pursuant to California Civil Procedure Code § 877, a good faith settlement bars a nonsettling defendant from seeking contribution from settling defendants, but the nonsettling defendant's liability is reduced by the settlement amount to the extent that all defendants are claimed to be joint tortfeasors. *McComber v. Wells*, 72 Cal. App. 4th 512, 516-17 (1999). As noted above, the settlement agreement explicitly allocated the settlement funds to malpractice claims and other specified claims distinct from the fraudulent transfer claim against Tramiel. Accordingly, it appears from the face of the settlement agreement that Tramiel may not obtain a settlement credit for any of the settlement funds. However, when it approved the settlement agreement, the bankruptcy court expressly reserved the right to determine

whether Tramiel was liable as a joint tortfeasor on any claim in the event Tramiel made a future request for settlement credit by Tramiel.

The trial went forward as against Tramiel approximately one year later. Tramiel did not request a finding of joint liability on any claim, nor did the bankruptcy court make such a finding. Based upon the allocation in the settlement agreement and the lack of any finding that Tramiel was a joint tortfeasor in the settled claims, the bankruptcy court stated explicitly in its original judgment that Tramiel was not entitled to a settlement credit.

Upon Tramiel's post-trial motion, the bankruptcy court entered an amended judgment on January 19, 2006, providing that Tramiel is entitled to a settlement credit in the amount of $4.5. In an opinion recited orally, the bankruptcy court stated that the second amended complaint made clear that all defendants were considered joint tortfeasors and conspirators. The court also noted that the settlement agreement indicated that only "the Trustee" had agreed to the agreement's allocation of settlement funds, and there was no evidence that the settling defendants agreed to this allocation. Finally, the court noted that it had reserved the right to allocate culpability amongst the defendants upon Tramiel's request for a credit.

The Trustee characterizes the bankruptcy court's conclusion that Tramiel is entitled to a settlement credit as a legal determination. Tramiel characterizes the issue as a factual one. This Court concludes that the issue presents mixed questions of law and fact. The Court further concludes that the determination that Tramiel is entitled to a settlement credit was clearly

erroneous. The integrated written settlement agreement clearly and expressly allocates the $4.5 in settlement funds to claims other than the claim upon which Tramiel was found liable. While the text of the settlement agreement does recite that "the Trustee" allocates the funds in this particular way, all of the settling defendants signed the integrated written settlement agreement, indicating their agreement to this term. There is *no* evidence in the record that any of the settling defendants disagreed with the allocation recited in the settlement agreement. The bankruptcy court clearly assumed that the allocation was valid at the time it approved the settlement, and expressly reserved authority to make a finding of joint liability as to the settled claims at Tramiel's request. There is *no* evidence in the record that Tramiel ever made such a request. Accordingly, this Court concludes that Tramiel is not entitled to a settlement credit.

B. Debt Relief

In 1996, JTS granted directors Tandon and Mitchell stock options to purchase one million shares of JTS common stock at an exercise price of $1 per share. They exercised their options, using full-recourse promissory notes with the stock pledged as security. Neither made any payments, and the notes were in default by spring 1997. By July 1997, the value of JTS stock had plummeted and the two million shares were worth less than the debt Tandon and Mitchell had incurred to purchase them. Tandon and Mitchell requested relief from these debts. The JTS board agreed.

The Trustee asserts that the debt relief was an illegal stock purchase under 8 Del. C. § 160, providing

in relevant part that "no corporation shall: (1) Purchase or redeem its own shares for cash or other property when the capital of the corporation is impaired." The Trustee asks that this Court hold Tramiel liable for Tandon's $1 million debt (it is unclear why the Trustee doesn't ask the same for Mitchell's debt).

The bankruptcy court made very explicit findings that the debt relief was *not* a purchase or redemption of shares, but rather an incentive for Tandon and Mitchell to stay with the company. This Court concludes that those factual findings were not clearly erroneous.

C. Repayment Of Atari Bridge Loan

In late 1997, JTS decided to sell certain intellectual property rights obtained in the merger with Atari. JTS needed interim financing to maintain its operations while it negotiated the sale. The Amber group, consisting of JTS shareholder Amber Arbitrage, Tandon, Mitchell and Tramiel, put up $3 million secured by the Atari intellectual property. In February 1998 JTS sold the intellectual property for $ 5 million, repaid the $3 million loan with interest, and had approximately $2 million more in cash than had been available several months previously. While conceding that the bridge loan in essence was an advance on the sale of intellectual property that enabled JTS to maintain operations for the months needed to consummate the sale, and that the transaction as a whole resulted in an additional $2 million in corporate funds, the Trustee asserts that the repayment of the $3 million was a breach of Tramiel's fiduciary duty and thus is void. Specifically, the Trustee asserts that

because JTS was insolvent at the time the $3 million loan was repaid, repayment of a loan to corporate directors ahead of other creditors was a *per se* breach of those directors' fiduciary duties under Delaware law.[1]

The bankruptcy court considered and rejected this theory and ultimately granted summary judgment for the defendants on this claim. The bankruptcy court's Summary Judgment Order set forth an extensive history of Delaware law relevant to interested director transactions, and concluded that even when the corporation is insolvent such a transaction is not *per se* void. Summary Judgment Order at 3-11. The bankruptcy court concluded that under Delaware law, the Trustee has the initial burden to establish the existence of an interested director transaction, and that once this burden is established, the defendants bear the burden of proving that the transaction was entirely fair to the corporation's creditors. *Id.* at 11. The bankruptcy court then concluded as a matter of law that based upon the undisputed facts in the record the Atari bridge loan and its repayment were entirely fair to JTS and its creditors.

Delaware case law does not provide a particularly clear road map with respect to interested director transactions in the context of corporate insolvency. This Court has reviewed the relevant authorities, dating back to the 1930s, and concludes that the legal

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[1] Claims against directors based upon the internal affairs of the corporation are governed by the law of the state of incorporation. *See In re Sagent Tech., Inc., Deriv. Litig.*, 278 F. Supp. 2d 1079, 1087 (N.D. Cal. 2003).

standard articulated by the bankruptcy court is the appropriate one and that the conclusion that the transaction was fair is well supported by the record.

IV. ORDER

The judgment of the bankruptcy court is AFFIRMED IN PART and REVERSED IN PART as follows:

(1) With respect to the real estate transaction, the bankruptcy court's judgment is AFFIRMED IN PART AND REVERSED IN PART; Tramiel is liable on the fraudulent conveyance claim in the amount of $6,714,370 plus prejudgment interest and is not entitled to a settlement credit;

(2) With respect to the debt relief transaction, the bankruptcy court's judgment is AFFIRMED; and

(3) With respect to the Atari bridge loan, the bankruptcy court's judgment is AFFIRMED.

DATED: 9/29/06

/s/ Jeremy Fogel
JEREMY FOGEL
United States District Judge

[*Certificate of Service omitted in printing*]

* * *

APPENDIX D

Entered on Docket
January 19, 2006
GLORIA L. FRANKLIN, CLERK
U.S BANKRUPTCY COURT
NORTHERN DISTRICT OF CALIFORNIA

The following constitutes
the order of the court. Signed January 19, 2006

Marilyn Morgan
U.S. Bankruptcy Judge

Jeffrey C. Wurms (Bar No. 124596)
Daniel Rapaport (Bar No. 67217)
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Suzanne L. Decker, Trustee

UNITED STATES BANKRUPTCY COURT
NORTHERN DISTRICT OF CALIFORNIA
SAN JOSE DIVISION

Case No. 98-59752 MM
Chapter 7

Adv. Pro. No. 00-5423

[Filed January 19, 2006]

In Re	)
	)
JTS CORPORATION,	)
	)
Debtor.	)
	)
SUZANNE L. DECKER, TRUSTEE,	)
	)
Plaintiff,	)
	)
vs.	)
	)
ROGER W. JOHNSON, et al.,	)
	)
Defendants.	)
	)

[Proposed] AMENDED JUDGMENT

The above case came on regularly for trial commencing April 4, 2005, in Room 3070 of the above-entitled Court, the Honorable Marilyn Morgan, Judge, presiding. Plaintiff Suzanne L. Decker, as trustee for the JTS Corporation bankruptcy estate ("Plaintiff"), appeared through her attorneys, Daniel

Rapaport and Jeffrey C. Wurms of Wendel, Rosen, Black & Dean LLP. Defendant Jack Tramiel ("Defendant") appeared through his attorneys, Christian B. Nielsen and Mai T. Buell of the Law Offices of Robinson and Wood.

Witnesses on the part of both Plaintiff and Defendant were sworn and examined. Documents submitted by both Plaintiff and Defendant were admitted into evidence. The Court heard the evidence submitted and also considered the trial briefs of the parties and the oral arguments and rebuttals of counsel. The Court retired to consider its decision.

Based on its September 30, 2005, Opinion Following Trial ("Opinion"), which sets forth its factual findings and legal analysis, and its order partially granting Defendant's Motion to Amend Judgment heard on December 22, 2005, the Court

ORDERS, ADJUDGES, AND DECREES as follows:

1. Defendant's purchase of real properties from the debtor is avoided as a constructive fraudulent transfer pursuant to 11 U.S.C. § 544(b) and California fraudulent transfer laws in the amount of $1,387,185;

2. Defendant's 11 U.S.C. § 550(a)(1) liability is $1,387,185, which amount is subject to prejudgment interest at the rate of 7% per annum, measured from the November 16, 2000, commencement of the within adversary proceeding, for a total liability of $1,859,133.30 through September 30, 2005, and an additional $266.04 per day thereafter;

3. Defendant may apply a settlement credit against the above liability for an amount equal to the $4.5 million of settlement payments made by Defendant's co-defendants. Plaintiff, therefore, may not recover any amount from the Defendant because the Defendant's liability is less than the amount of the settlement credit.

4. Defendant is not entitled to receive a credit or an offset for his indemnity claim.

5. Defendant's interest in the blanket lien placed against JTS's assets as part of the NationsBanc transaction is avoided as an actual fraudulent transfer pursuant to 11 U.S.C. § 548; and

6. Defendant is entitled to judgment in his favor on all of Trustee's remaining claims. WHEREFORE, this judgment confirms the Court's findings.

Certificate of Service: Docket No 583

*** * * END OF ORDER * * ***

[*Court Service List omitted in printing of this appendix*]

* * *

APPENDIX E

Entered on Docket
October 3, 2005
GLORIA L. FRANKLIN, CLERK
U.S BANKRUPTCY COURT
NORTHERN DISTRICT OF CALIFORNIA

The following constitutes
the order of the court. Signed October 3, 2005

Marilyn Morgan
U.S. Bankruptcy Judge

UNITED STATES BANKRUPTCY COURT
NORTHERN DISTRICT OF CALIFORNIA

Case No. 98-59752-MM
Chapter 7

Adv. Proc. No. 00-5423

[Filed October 3, 2005]

In re:	)
	)
JTS CORPORATION,	)
	)
Debtor.	)
	)
SUZANNE L. DECKER, Trustee,	)
	)
Plaintiff,	)
	)
v.	)
	)
DAVID T. MITCHELL, JACK TRAMIEL, SIRJONG LAL "JUGI" TANDON, COOLEY GODWARD, LLP, MATTHEW W. SONSINI, ANDREI M. MANOLIU and ANNA B. POPE,	)
	)
Defendants.	)

OPINION FOLLOWING TRIAL

INTRODUCTION

The trustee's second amended complaint against JTS's directors, its attorneys and a major shareholder asserts claims for breach of fiduciary duty, preference, fraudulent conveyance, equitable subordination, avoidance of transfers, illegal redemption of shares, legal malpractice, alter ego liability, unfair business practices, aiding and abetting liability, and conspiracy. Through various motions filed by the parties, I eliminated some claims and determined the applicable choice of law. Subsequently, I also addressed the

application of Delaware's trust fund doctrine to this case, indicating that many factual issues remained for trial. *Decker v. Mitchell (In re JTS)*, 305 B.R. 529 (Bankr. N.D. Cal. 2003). Only one defendant remains. The issues for determination involve whether JTS was insolvent at the relevant times, whether the sale of real property to Tramiel is avoidable as a constructive fraudulent conveyance, whether Tramiel breached fiduciary duties through alleged violation of the fairness requirements of the trust fund doctrine, whether Tramiel violated California's unfair competition law, whether JTS violated Delaware's requirement that a corporation not repurchase or redeem its own shares while its capitol is impaired, and whether a blanket lien given by JTS is an actual fraudulent conveyance. In addition to liability questions, there remain issues concerning the right to indemnity, settlement credits, and prejudgment interest.

FACTS

JTS Corporation was formed in 1994 to design, manufacture, and market a smaller, slimmer hard disk drive to be used in personal computers. JTS entered into a long term contract with Compaq to develop a 3" disk drive that would be compatible with a new notebook computer that Compaq was developing. After JTS was unable to meet Compaq's quality standards, Compaq terminated the contract, which produced a domino effect with JTS's other business prospects. By 1996, the products that JTS had in distribution and in development were of little value, and the company needed additional working capital to overcome this set back.

In early 1996, JTS determined that it was not strong enough to go public as a means to raise capital and, instead, agreed to merge with Atari corporation to obtain much needed funds. Following the agreement to merge, Atari loaned JTS $25 million, which was expected to see the company through September of that year. Through the merger, JTS further acquired $15 million in cash, $55 million attributable to intellectual property, and eight real properties with a book value of $10 million.

In addition to the transfer of assets, the merger brought Jack Tramiel, Atari's chairman of the board, to the JTS board of directors. Tramiel, who himself had served on two other corporate boards, joined a group of directors who, in their own right, were sophisticated businessmen. For example, Jugi Tandon, the chairman of JTS's board, had many years of experience in the disk drive industry including time spent with Memorex Products, Inc. and as founder and chief executive officer of Tandon Corporation. David Mitchell, the President and chief executive officer of JTS, had previously served as an officer and director for Seagate Technology, Inc. and Connor Peripherals, Inc. Roger Johnson had over twenty years experience in the disk drive industry both with Memorex and with Western Digital Corporation, a company where he served as chairman of the board and chief executive officer. Lip-Bu Tan, while a venture capitalist by trade, had significant experience at the corporate board level. His investment banking firm always placed one of its members on the board of the companies in which it invested. Over the years, he has served as a director of at least ten to twenty companies. Like Tan, Jean DeLeage was a venture capitalist. However, he too had served on other boards both prior to and after JTS,

including the board of Tandon Corporation along with Jugi Tandon.

By the time the merger closed on July 30, 1996, JTS's debt exceeded its assets by $23 million, and it continued to burn through cash to fund production. Again, the company needed to raise additional money and to do so quickly because the $25 million loan from Atari was nearly depleted. To satisfy its demands, the company turned to liquidating the real and intellectual property acquired from Atari. While the additional Atari assets allowed JTS to continue for a period of time, by July 1997, the disk drive market was glutted and sales plummeted. To survive, JTS's board of directors decided to abandon production of a smaller disk drive and instead to pursue a new business model based on a very low-cost, high-capacity disk drive. Management pitched the new business model to JTS's vendors and creditors, who agreed to give JTS the opportunity to implement the new model. Despite management's efforts, however, the company was unable to recover. On November 17, 1998, the company was forced into bankruptcy through an involuntary petition. JTS then filed a voluntary petition for relief under Chapter 11 on December 4, 1998, scheduling assets of $4.2 million and liabilities of $136 million. The case converted to Chapter 7 on January 29, 1999.

Three transactions that took place after the JTS - Atari merger, but before bankruptcy, serve as the basis for the trustee's claims against Tramiel. Facts regarding each transaction are set forth below.

Real Property Transaction

In mid-1996, following board approval of the Atari merger, JTS continued to search for new sources of cash to fund its development and production of disk drives because the cash from Atari was only expected to fund operations through September. Virginia Walker, the company's chief financial officer, talked to Tramiel, who introduced her to a number of investment bankers. After her efforts proved fruitless, Walker turned to the eight parcels of real property that JTS would eventually acquire from Atari as a potential source of funds. The properties, which were located in California and Texas were surplus property. They would not be part of JTS's day to day operations and had nothing to do with the company's technology business. Because the properties were unencumbered by liens, they were an available source of cash.

Walker approached Tramiel to see whether he had any interest in buying the portfolio. Tramiel, who, as chairman of Atari, was familiar with the property, responded with a proposal to buy the entire portfolio for its book value of $10 million, with JTS retaining an option to repurchase the portfolio for the same $10 million during the first year following the sale. If JTS exercised its option, however, Tramiel would keep the greater of $1 million or the rental income generated by the properties during the twelve month option period. Tramiel proposed these terms because he believed that the one year option period would protect the company by allowing it to find a buyer that might offer a higher price while his ability to retain at least $1 million of rental income would approximate the return on investment that he would have earned from any investments liquidated to buy the real estate.

Around this same time, Walker also contacted Andre Manoliu, an attorney with Cooley Godward, LLP who represented JTS. Walker told Manoliu that the company needed cash right away and asked for his advice concerning the potential sale of the real property. Manoliu recalls that he advised Walker that the board needed to approve the sale, that she needed to present the board with some indication of the properties, but that a repurchase option was a good way to allow for a quick sale and still protect the assets' value to the company over time.

At a June 18, 1996 JTS board meeting, Walker formally proposed the idea of selling the real properties to Tramiel. The board minutes establish that, after a full discussion of the matter, the board authorized Walker to work with Manoliu to implement the proposed sale. Testimony of the former directors confirms that the board thoroughly addressed the matter. Although the directors no longer remember the specific date of any discussions or any formal board resolution, they recall discussing and agreeing with the potential real estate sale to Tramiel. The weight of the evidence demonstrates that board was sensitive to the fact that, as an interested director transaction, the sale needed to be fair. Jean DeLeage recalls a discussion that JTS might receive better value under other circumstances but, in light of JTS's immediate need for cash, Tramiel's offer was fair. Manoliu testified that he and Walker discussed the repurchase option with the board and that the board viewed the option period as a protective mechanism that would give the board sufficient time to further analyze the value of the real estate and make an informed decision as to whether the option should be exercised. The sum of the evidence indicates that the board agreed with

the transaction and relied on counsel to assess the propriety of the details. Although expert testimony at trial showed that JTS might have been able to borrow against the eight properties, the testimony of the former board members was skeptical at best. Moreover, JTS's chief executive officer preferred to have the company's available assets in cash. The weight of the evidence establishes that the board believed that the sale of the real estate was the fastest and best means to obtain the cash needed to fund operations.

Throughout the process, Tramiel abstained from all votes concerning the sale and removed himself from the boardroom whenever the transaction was discussed. Former board member DeLeage recalls that Tramiel's demeanor throughout the process was above board and that Tramiel even told the board that they should get an independent assessment of the value of the property. There is no evidence that Tramiel provided the board with any information concerning the value of the eight properties prior to closing the transaction. Indeed, Tramiel believed that he had no duty to disclose such information once he became the buyer. Tramiel testified that, as part of the merger negotiations, he may have told Manoliu that the properties were worth $12-13 million but, at that time, he was bargaining with JTS for the best deal possible. Tramiel testified that when he bought the real properties, he was not aware of any appraisals valuing the portfolio of properties at more than $10 million. On the other hand, communications between Walker and Anna Pope, the Cooley Godward attorney assigned to document the transaction for JTS, establish that JTS had access to information suggesting that the

aggregate value of the eight individual parcels might be as high as $14-$16 million.

After JTS's board agreed to the basic terms that Tramiel had proposed, attorneys for each party finalized the details and drafted the necessary documentation. The sale closed in September 1996. Tramiel purchased the property without financing or inspections and subject to all title defects. Although JTS paid all expenses associated with the transaction, by selling to Tramiel, the company avoided paying any broker's commission. During the twelve month option period, Tramiel was required to cooperate with JTS in marketing the properties and was prohibited from encumbering, altering or selling the properties without JTS's consent.

In June or July 1997, Eugene Hill, JTS's Treasurer, first began JTS's efforts to market the portfolio of real property. Although two entities expressed interest in a portion of the portfolio, both indicated that they wanted an extension of the option period before they would consider making a serious offer. Hill contacted Garry Tramiel, Jack Tramiel's son, who managed the eight properties during the option period. Hill requested an extension of the option period, explaining that there was a prospective buyer that could be serious if given an extension. A week later, Garry responded that his father was not interested in extending the option because there was no real offer on the table. Tramiel confirmed that he did not extend the option because there was no serious offer to buy the entire portfolio; there was nothing more than an expression of interest in one of the parcels.

The parties stipulated that the properties generated net rental income of $1,387,185 during the option period. Tramiel's belated attempt to be released from that stipulation was unconvincing. Garry Tramiel testified that the net income from the properties during the September 1996-September 1997 option period was only in the range of $960,000 based only on his recollection from a decade ago, as well as a 1994-95 summary of rental income and property tax information. In addition to the summary being from a different time period, Garry Tramiel conceded that he did not know who prepared the summary and he did not know if the numbers contained within it were entirely accurate. The option period expired at the end of the first twelve months without being exercised. Ultimately, Tramiel transferred the portfolio of property to an entity for the benefit of his children.

Debt Relief Transaction

Sometime in 1995, Mitchell purchased two million shares of JTS stock at .25¢ per share, or $500,000. He paid JTS with a $400,000 promissory note and the balance in cash. In early 1996, shortly after the JTS Atari merger was approved but before it closed, the JTS board granted Mitchell and Tandon stock options to purchase one million shares each of JTS common stock at an exercise price of $1 per share. Both Mitchell and Tandon exercised the options, using full-recourse promissory notes with the stock pledged as security. As a result of these transactions, Mitchell and Tandon owed JTS $1.4 million and $1 million, respectively. Because neither Mitchell or Tandon made any payments, the notes were in default by spring of 1997.

The JTS board granted the stock options to reward Mitchell and Tandon for their work on the merger and as an incentive for these two key executives, who would benefit as the stock increased in value. Testimony from JTS's former directors establishes that the members of the board believed that Mitchell and Tandon's involvement was crucial to JTS's success. Tramiel stated that, without Mitchell and Tandon, there would not have been a company, and Tramiel's respect for the abilities of these men was one of the main reasons that Tramiel agreed to merge Atari into JTS. Roger Johnson similarly described Mitchell and Tandon as critical to JTS's operations.

However, by July 1997, when both disk drive sales and the value of JTS stock were plummeting, the two million shares of $ 1 stock that Mitchell and Tandon had purchased, were worth less than the debt they had incurred to purchase them. The stock no longer provided an incentive; rather, the debt owed for the stock had become a financial burden. Around the same time, in an effort to turn the company around, JTS made the decision to adopt a low cost, high capacity disk drive as its new business model. Mitchell and Tandon were trying to persuade JTS's vendors and creditors to work with the company as it executed this shift. According to Tramiel, Mitchell's and Tandon's experience in the disk drive industry was pivotal to implementing the new model. It was important to keep Mitchell and Tandon happy because the company could not function without them. These men were everything. It was in this atmosphere that Mitchell and Tandon asked JTS to consider reducing the debt that they owed to the company.

While no one recalls the precise date when Mitchell and Tandon first raised the issue of debt relief, notes from July 1997 indicate that they had a discussion with Matthew Sonsini, a Cooley Godward attorney, early that month. Tramiel recalls that the debt relief issue came to the board's attention in that same time frame. Manoliu recalls several discussions at the board level beginning in the July 1997. Regardless of the precise dates of any discussions, the evidence is clear that the main concern of the board was to provide Mitchell and Tandon incentive to stay on with JTS.

Manoliu specifically recalls discussions at a board meeting where concerns were expressed about retaining Mitchell and Tandon, because the stock that was originally intended to compensate Mitchell and Tandon had turned out to be a liability and, otherwise, their overall compensation was not that high. Manoliu recalls that the board wanted to provide the debt relief as new incentive to Mitchell and Tandon and as consideration for them to stay on for several months or a year. Similarly, Tramiel recalls that Mitchell said he was "in a jam" because of the debt. Although neither Mitchell or Tandon explicitly threatened to leave the company if no relief was provided, Tramiel remembers that the look on their faces and the tone of their discussions indicated that they might. Tramiel voted in favor of debt relief because it was a small price to pay to ensure that these pivotal executives would take the company forward. Johnson also recalled one or more discussions of debt relief that took place in the JTS boardroom. As a result of those discussions, Johnson believed that, absent relief, Mitchell and Tandon might decide to leave. At the very least, the debt had become a distraction to both Mitchell and Tandon at a time when these men were under a lot of

pressure managing JTS. He believed that Mitchell and Tandon would not be able to focus on the company without relief and that an implicit part of the agreement to provide debt relief was the continued commitment of Mitchell and Tandon to stay on with JTS. Although Tandon does not recall the debt relief being conditioned on his continued employment, Mitchell's understanding was that the board agreed to forgive his debt to JTS if he stayed on to implement the company's new business model.

On July 17, 1997, the debt relief for Mitchell and Tandon was one of several topics discussed at a JTS board meeting. Prior to the debt relief discussion, both Mitchell and Tandon left the boardroom. As a result, it appears that Tramiel and Johnson, along with Joe Prezioso, who succeeded Walker as JTS's chief financial officer, and Sonsini participated in the discussion. While Sonsini's handwritten notes from the board meeting document approval of the note cancellations, they do not reflect any details regarding the structure of the transaction. Based on the evidence before me, the most reasonable explanation for the lack of detail was the continuing need to have legal counsel research and determine an appropriate mechanism for providing the approved debt relief. On this point, Manoliu's testimony was forceful and persuasive. While Manoliu's memory of the details regarding each meeting has, understandably, faded, he was adamant that, after the July 1997 board meeting, Cooley had very clear marching instructions from the board. Cooley was to complete the debt relief transaction but only if it could be structured so that the board members would have no personal exposure. Likewise, Sonsini recalls that after the meeting where cancellation of the notes was approved, he was to

research the best structure for the transaction and discussions about the appropriate mechanism were ongoing. Both attorneys remember that the exact form of the relief was not resolved until several months later. Consistent with the attorneys' recollection, Tramiel testified that he agreed to the concept of debt relief, but that he did so with the expectation that Cooley Godward would work out the details to ensure that the transaction was legal and without adverse consequences. From the discussions he recalled, Johnson believed that Mitchell and Tandon would need to return their stock in exchange for the debt forgiveness, but he also understood that the attorneys were working out the details.

The paper trail regarding Mitchell and Tandon's debt relief corresponds with the recollections of the people involved in the debt relief transaction. Although Sonsini prepared a memorandum to the board dated July 17, 1997 outlining a potential proposal to repurchase Mitchell's and Tandon's shares in exchange for the debt forgiveness, the evidence is not clear whether this memorandum was actually presented to the board. Attorney Sonsini's handwritten notes from the July 17, 1997 meeting establish only that the board approved the cancellation of the loans for the $1 stock and the forgiveness of interest on Mitchell's $.25 stock. There is no indication that the cancellation of the notes was to be in exchange for the return of the stock.

Following the July 17, 1997 meeting, Sonsini's notes document his continued research into the best means to provide debt relief. At one point, he had a conversation with an attorney in Delaware where he learned that a repurchase of Mitchell and Tandon's

shares could be problematic and result in liability for JTS's board members. Sonsini explored other ways to provide the debt relief that the board had approved. His notes show that recession of the transactions and JTS's ability to void the transactions were considered. Ultimately, in early 1998, he concluded that the debt relief was best structured as additional compensation to Mitchell and Tandon for their continued service to JTS, a structure that was consistent with the board's original intent in approving the debt relief. Manoliu recalls that Cooley informed the board that it had resolved the issue of how to accomplish the debt relief.

Because the evidence before me indicates that, from the outset, JTS intended the debt relief as an incentive to Mitchell and Tandon to encourage them to stay with JTS and pull the company through an extremely rocky time, I do not infer any nefarious intent from the fact that the minutes of the July 17, 1997 board meeting may not have been finalized until sometime in 1998. Significantly, no one recalls anything unusual about the preparation of the minutes, and Manoliu testified that corporate minutes are sometimes prepared over time. Here, the evidence shows that JTS's legal counsel spent many months setting up the debt relief transaction to meet the board's expectations and approval. While JTS might have been able to prepare minutes to reflect the board's referral of the issue to legal counsel, I am not persuaded that waiting to prepare the minutes until the structure of the transaction was finalized is evidence of a cover-up as the trustee has asserted.

NationsBanc Transaction

JTS began implementing its new business model mid-way through 1997. Nevertheless, its situation remained precarious into the fall of that year. In the final quarter of 1997, JTS began to show a profit and appeared to be on the brink of turning the corner to profitability. To maintain its forward momentum, however, JTS needed more cash to continue its operations.

In September 1997, Amber Arbitrage, one of JTS's major shareholders, agreed to invest an additional $20 million in the company, but only if the JTS board of directors made a show of good faith by participating in the financing with an additional $5 million. Some of JTS's directors declined to participate due to their affiliation with venture capital funds. However, Tramiel, Mitchell and Tandon agreed to invest. Tramiel credibly testified that he did not want to be involved in the deal, but when he was approached, he agreed to invest an additional $3 million because he knew JTS needed the money to survive. Tramiel also believed that Amber's willingness to invest $20 million was a positive sign and that the additional $3 million was not particularly significant in light of the much larger amount he had already invested in JTS. Tramiel described his role in the transaction as akin to a minority shareholder. He was not aware of the details because Amber was calling all the shots.

Amber, along with the director participants, placed a total of $25 million in an escrow account at Cooley Godward. JTS established a second escrow account at Cooley that contained JTS Series D preferred stock that was valued at $25 million. Each Series D share

was convertible to 5,000 common shares at an additional conversion price of $ 0.65 per share. As part of the transaction, the director participants gave Amber exclusive authority to release funds from the cash escrow. Whenever Amber permitted JTS to draw funds out of the cash escrow, Amber and the director participants received a corresponding amount of Series D stock in exchange.

By November 1997, Amber had authorized the release of just over $ 13.4 million from the cash account and 15,313 shares of Series D stock, worth approximately $13.4 million, had been issued on a pro rata basis to Amber, Mitchell, Tandon and Tramiel. Around this same time, JTS management, specifically Prezioso, its chief financial officer, expressed concern that JTS's vendors were trying to attach JTS's assets to collect the money that JTS owed to them. On November 10, 1997, Prezioso spoke with Pamela Martinson, an attorney at Cooley Godward, about obtaining protection from creditors by putting investors in place who would have a blanket security interest in JTS's assets. At trial, Ms. Martinson explained that senior security interests are commonly used to keep order among a company's creditors. Prezioso advised Martinson that the transaction with investors needed to appear to be a real transaction. That same day, Martinson spoke with Mitchell and Manoliu about using the funds in the cash escrow as a loan against account receivables. Ms. Martinson's notes reflect that JTS and Amber spent the remainder of November trying to work out the details of a loan from the escrow account.

During the month of November, however, the price of JTS commonstock fell far below the conversion price

of the Series D preferred stock. The Series D convertible shares became "deep out of the money" because common stock could be purchased on the open market for much less than the cost of converting the Series D shares. As a result, the Series D shares were close to worthless. This state of affairs made Amber nervous and led to its refusal to release any additional funds from the cash escrow at Cooley. JTS was forced to seek out other sources of funds.

Ms. Martinson's notes from December 4, 1997 reveal that she discussed the idea of bank financing through NationsBanc with Prezioso that day. NationsBanc and Amber had come to JTS with a proposal. NationsBanc was willing to provide a $10 million line of credit to JTS based on a factoring agreement, if Amber would use a portion of the remaining funds in the cash escrow to provide NationsBanc with collateral for the credit line. Before Amber was willing to authorize use of the cash escrow, however, it wanted JTS to re-price the Series D stock that was out of the money. From Tramiel's perspective, Amber and NationsBanc were acting as one entity. Tramiel and the other director participants had no control over the transaction, and because of their interest, they did not participate in board level discussions about the transaction.

To access the $10 million from the escrow account, JTS agreed to reprice Amber's preferred stock, by exchanging newly issued Series E preferred stock for the Series D stock on a share for share basis. The Series E stock was virtually identical to the Series D shares except that the price to convert to 5,000 shares of JTS common was lowered to $0.10 per Series E share. The exchange of the Series E shares for the

Series D stock took place on December 17, 1997. Although the record does not reflect a formal board resolution authorizing the exchange, Manoliu was certain that the board had discussed and approved it.

Between December 1997 and February 1998, the NationsBanc credit facility was finalized. The terms of the factoring contract were negotiated by NationsBanc and counsel for Amber. Amber released funds from the cash escrow to purchase $10 million in certificates of deposit to secure the NationsBanc loan. JTS also provided NationsBanc with a senior blanket lien on all of JTS's assets. Ms. Martinson's notes from a January 1998 telephone conversation specifically indicate that Prezioso asked her to make sure that all of JTS's assets served as collateral for the NationsBanc loan. She understood that the purpose of the blanket security interest was to accomplish an orderly distribution of assets for all creditors. Amber's counsel also negotiated for and received a second priority blanket lien in favor of Amber, Tandon, Mitchell and Tramiel to the extent that the certificates of deposit were drawn down. When JTS defaulted on the NationsBanc loan, NationsBanc drew down on the certificates of deposit securing the loan. Amber, Tandon, Mitchell and Tramiel became surrogate to the NationsBanc lien.

CONCLUSIONS OF LAW

I. JTS Was Insolvent When Each of the Three Relevant Transactions Took Place

The Bankruptcy Code defines insolvency for a corporation as a financial condition where "the sum of [the corporation's] debts is greater than all of [its]

property, at a fair valuation." 11 U.S.C. § 101(32(a). Based on this definition, the uncontroverted testimony of the trustee's economic expert, Kevin Kreitzman, establishes that JTS was insolvent from early 1996 forward. Using two separate methodologies, Kreitzman undertook an analysis of JTS's solvency beginning with 1996. He used the balance sheet test set forth in the Code, which compares assets against liabilities to see whether the company's total debt exceeded its total assets. He also considered JTS's ability to pay its debts as they became due. Under either method, Kreitzman determined that JTS was insolvent as early as 1996. From that point forward, JTS's financial condition only deteriorated. By the time of the merger with Atari, Kreitzman noted that JTS's liabilities exceeded its assets by $23 million. As a result, Kreitzman opined that JTS was insolvent in 1) September 1996, when the real properties transaction closed; 2) July 1997, when the debt relief transaction took place; and 3) December 1997, when the NationsBanc transaction occurred. Kreitzman's conclusions are consistent with the testimony of JTS's former officers and directors who described a business climate where JTS took on a risky and ambitious plan just as the disk drive market experienced a sudden downturn. By 1996, JTS's inventory of disk drives had little to no value and its debt to trade vendors was mounting.

Tramiel offered no evidence of solvency. The uncontroverted evidence establishes that JTS was insolvent from September 1996 forward during each of the transactions.

II. The Real Properties Transaction

A. The Sale of the Real Properties to Tramiel Is Avoidable as a Constructive Fraudulent Conveyance

Because § 548 of the Bankruptcy Code, which allows a trustee to avoid certain transfers of a debtor's property, only applies to transfers that occur within a year of the petition date, the trustee must rely on § 544 of the Code to avoid the sale of the real properties. Section 544(b) allows a trustee to avoid transfers of a debtor's property that would be avoidable under state law. Under California's fraudulent conveyance laws, a transfer is avoidable if the debtor made the transfer without receiving a reasonably equivalent value in exchange for the transfer and the debtor intended to incur, or believed or reasonably should have believed that it would incur debts beyond its ability to pay as they become due. Cal. Civ. Code § 3439.04(b). The ninth circuit has recognized that, but for the one year temporal limitation found only in the Code, California's fraudulent conveyance statutes are similar in form and substance to the Code's fraudulent conveyance provisions and generally can be analyzed as one. *Wyle v. C.H. Rider & Family (In re United Energy Corp.)*, 944 F.2d 589, 594 (9th Cir. 1991). So, to avoid the real properties sale as a fraudulent transfer under § 544 and California law, the trustee must establish that: 1) a transfer of debtor's property occurred; 2) the debtor did not receive reasonably equivalent value in exchange; and 3) the debtor was insolvent, was made insolvent by the transaction, was operating or about to operate without property constituting reasonably sufficient capital, or was unable to pay debts as they

become due. *Id.* The only disputed issue is whether Tramiel gave JTS reasonably equivalent value in exchange for the portfolio of property.

Reasonably equivalent value must be determined from the standpoint of a debtor's creditors, not from the defendant's perspective. *In re Prejean*, 994 F.2d 706, 708 (9th Cir.1993). Because the policy of § 544 is to preserve assets of the estate, the focus is on the net effect of the transfer on the debtor's estate and on the funds available to the unsecured creditors. *Frontier Bank v. Brown (In re Northern Merchandise, Inc.)*, 371 F.3d 1056, 1059 (9th Cir. 2004), *United Energy*, 944 F.2d at 596. The analysis must compare what the debtor surrendered against what the debtor received, irrespective of what any third party may have gained or lost. While fair market value is one factor to be considered, in the end the determination of an asset's value or of the consideration paid is a factual inquiry that should account for all the specific circumstances of each case. *In re Dullea Land Co.*, 269 B.R. 33 (8th Cir. B.A.P. 2001); *In re Fairchild Aircraft Corp.*, 6 F.3d 1119, 1125, n.5 (5th Cir. 1993).

To determine whether JTS received reasonably equivalent value in exchange for the sale of the portfolio of eight properties, I must first ascertain the value of the property that JTS transferred, as of the date of the transfer, September 9, 1996. *In re Ozark Restaurant Equipment Co., Inc.*,850 F.2d 342, 344-45 (8th Cir. 1988). The parties each offered expert testimony on this issue. For purposes of their opinions, the experts agree that the eight properties had an aggregate value of $ 15,760,000, if the properties were sold individually after being exposed to the market for as much as one year. However, the experts disagree as

to whether that value should be discounted because the properties were sold as a bundled portfolio or because the sale took place within a short period of time - sixty days. Assuming any discount is appropriate, the experts disagree as to the amount of the discount to be applied.

After careful consideration of the presentations by both experts, I conclude that a 20% discount for bundling the properties is appropriate and that a further 5% discount should be applied for the quick sale. Even the trustee's expert, Charles Dannis, recognized that discounts for a bulk sale and a quick sale would be appropriate if a seller insisted on those terms. This makes sense because the buyer accepts the risk of less attractive properties that are bundled with the more valuable pieces and because the seller loses the competitive benefit of a normal marketing period. Although the trustee asserts that no discount should apply because Tramiel, not JTS, insisted on the purchase of the entire portfolio and there was no economic need to complete the sale within sixty days, the evidence establishes that JTS wanted both a bundled sale and a quick sale. It was JTS that first proposed the sale of the portfolio to Tramiel. While Tramiel may have declined to consider splitting out the sale of one of the more valuable individual properties after the terms of the transaction had been fixed, JTS set the original tone of this transaction as bundled sale. JTS's chief executive officer preferred to have the company's available assets in cash. Moreover, by summer of 1996, JTS had been insolvent for some months and its financial condition was deteriorating rapidly. The company needed cash and needed it quickly to fund continued operations. The bridge loan from Atari to JTS was only expected to last until

September 1996 - the same month that the sale of the properties closed. JTS was willing to accept something less than the best price to get cash fast. Under these circumstances, both a bundled sale and a quick sale discount is appropriate.

The next question is what discount is suitable under the facts at hand. The trustee's expert testified that a 5.5% bulk discount should be applied based on his conversations with four companies that purchased bulk properties in the 1996 time frame. Tramiel's expert, John Ellis, concluded that a significantly larger, 20-30%, discount was more fitting. To reach his conclusion, Ellis performed historical research and discovered that, in the early 1990's, the Resolution Trust Corporation had allowed as much as a 50% discount when it sold properties as a bundle. Ellis also interviewed representatives from two companies that represented bulk investors during 1996 and each believed that a 25-30% discount would not be out of line. On balance, Tramiel's expert was more persuasive on this point and, because of Tramiel's familiarity with the portfolio, I accept 20%, the low end of Ellis's range, as the correct bulk sale discount in this case.

Ellis also testified that it is reasonable to expect that property exposed to the market for less than one year will bring in a lower sales price between a willing buyer and seller. Although he believed that the discount should be substantial for the quick sale aspect, he had no opinion as to the correct amount. The trustee's expert testified that if a quick sale discount were to apply, he would discount the value by 1% for each month short of an average seven month marketing period, or here, a total of five percent.

Based or this evidence, it is reasonable to apply a 5% discount related to the absence of a standard marketing period for the portfolio of properties. Applying both discounts to the uncontroverted aggregate value of the individual properties, I conclude that the fair value of the portfolio sold to Tramiel was $11,820,000.

Turning to the question of what JTS received in exchange for the property, there is no dispute that JTS received $10 million in cash. The question whether JTS received reasonably equivalent value then turns on the worth of the one year repurchase option that Tramiel also gave to the company. The trustee presented expert testimony that the repurchase option had no economic value to JTS because the board of directors never had any actual knowledge of the portfolio's fair market value and because the option ultimately lapsed, providing no value to JTS's creditors. These arguments are flawed because they are based on hindsight. I must determine the value of the consideration received as of the time the transfer occurred, not with the benefit of hindsight. *In re Next Wave Personal Communications, Inc.*, 200 F.3d 43, 49 (2d Cir. 1999). In September 1996, JTS had both the ability to determine the fair market value of the properties and to exercise the option. The fact that JTS did not take advantage of these opportunities after the sale closed does not change the value of the consideration received.

Tramiel's expert testified that, except for extreme cases, the value of a repurchase option is equal to the difference between the fair market value of the property and the strike price of the option. I am persuaded that, in most cases, this is an appropriate

formula for valuing a repurchase option, but I disagree with Tramiel's application of the formula to the facts of this case. In *In re Cavillo*, 263 B.R. 214 (W.D. Tex. 2000), the district court was asked to value an option to repurchase. It concluded that, in the case before it, the appropriate value of the option was the fair market value of the property minus the fixed strike price of the option. *Id.* at 220. There, the strike price to regain possession of the property transferred was substantially higher than the original purchase price, one means of providing a buyer with a return on its investment in the event the option is exercised. Here, by contrast, the contractually stated strike price for the option is identical to the original purchase price. Nevertheless, the parties built in protection for Tramiel by allowing him to retain the greater of $1 million or the first twelve months of rental income from the properties if JTS decided to exercise its option. Thus, to exercise the option, JTS not only had to pay $10 million, it also had to relinquish all rights it had to $1,387,185, the option year's net rental income from the properties. Under these circumstances, the loss of the rental income should be added to the fixed $10 million for an actual strike price of $11,387,185. Subtracting that strike price from the fair market value of $11,820,000, the option has a value of $432,815. The option value must then be added to the $10 million cash paid to produce total consideration to JTS of $10,432,815.

Based on the above calculations, the total consideration that JTS received is $1,387,185 less than the value of the property it sold. In the fraudulent conveyance context the statutory phrase "reasonably equivalent value" has been recognized to mean the approximate equivalent of a property's fair market

value. *BFP v. Resolution Trust Corp.*, 114 S. Ct. 1757, 1765 (1994); *Northern Merchandise*, 371 F.3d at 1059. In light of the substantial difference between the consideration received and the properties' fair value, I conclude that JTS did not receive reasonable equivalent value for the properties and the transaction is avoidable as a fraudulent conveyance.

When a transfer is avoided under § 544 based on state law avoidance powers, § 550 of the Bankruptcy Code governs the liability of the transferee. Based on § 550, which provides that the trustee may recover the property transferred or the value of that property, the trustee urges that the estate is entitled to recover the full fair market value of the property, $11,820,000, without any reduction for the consideration that Tramiel paid. Acknowledging that Cal. Civ. Code §3439.08(d) normally provides a good faith transferee who had his transfer avoided under California law with a reduction in the amount of liability based on the value given for the property, the trustee contends that this reduction is unavailable when the avoidance takes place pursuant to the Bankruptcy Code § 544. She argues that § 544 incorporates state fraudulent transfer law, but not the state law recovery procedures set out in § 3439.08.

The trustee has misconstrued the California fraudulent conveyance statutes. Under Cal. Civ. Code § 3439.07(a)(1) the ability to avoid a transfer is expressly subject to the limitations set forth in § 3439.08. Because § 544 merely allows a bankruptcy trustee to assert avoidance powers that are otherwise available under state law, here, the trustee may only avoid the real properties sale to extent permitted in § 3439.07. One express limitation on the ability to

avoid a transfer is a transferee's good faith defense. *See* Cal. Civ. Code § 3439.08(d)(3). Under § 3439.08(d)(3), a good faith transferee is entitled, to the extent of the value given the debtor for the transfer, to a reduction in the amount of liability on the judgment. § 3439.08(d)(3). Under the plain language of California fraudulent conveyance laws, if Tramiel is a good faith transferee, the transaction may only be avoided to the extent that the value of the real properties exceeded the value that Tramiel gave to JTS.

Good faith, for purposes of § 3439.08(d)(3), requires an honest belief in the propriety of the activities in question and no deliberate wrongful conduct to take advantage of others. *Lewis v. Superior Court*, 30 Cal. App. 4th 1850, 1859 (1995). Here, there is no evidence that Tramiel intended to take advantage of JTS when he purchased the portfolio of real property. Rather, the evidence is overwhelming that Tramiel honestly believed that he was helping the company by allowing it to get immediate access to cash, while protecting it if JTS could ultimately find a buyer willing to pay a higher price. Based on the circumstances before me, the trustee may only recover the difference between the value of the property transferred and the value of the consideration that Tramiel paid - $1,387,185.

B. Tramiel Did Not Breach His Fiduciary Duties to JTS When He Purchased the Real Properties

As explained in my decision on the parties' motions for summary judgment, Delaware's trust fund doctrine, which governs the trustee's breach of fiduciary duty claims, does not compel a finding that

Tramiel breached his fiduciary duties to JTS simply because the portfolio of properties was conveyed to him for less than fair market value. However, the real estate transaction was a self-dealing transaction, and a breach of fiduciary duty can occur if a director exploits his fiduciary position for personal gain even if not at the corporation's expense. *Cantor v. Perelman*, 414 F.3d 430, 435 (3d Cir. 2005). As a result, the burden falls on Tramiel to establish that the transaction was entirely fair to the corporation's constituent groups at the time it took place. *In re JTS Corporation*, 305 B.R. 529, 541 (Bankr. N.D. Cal. 2003). The proof must pass careful scrutiny. *Weinberger v. UOP, Inc.*, 457 A.2d 701, 710 (S. Ct. Del. 1983). Tramiel must demonstrate his utmost good faith and the most scrupulous inherent fairness of the bargain. *Marciano v. Nakash*, 535 A.2d 400, 404 (S. Ct. Del. 1987). An interested director is presumed to have acted in his own self-interest absent proof that the transaction is fair. *JTS*, 305 B.R. at 541.

To determine fairness, I must examine all facets of the real estate transaction, keeping in mind that whether a transaction is entirely fair does not lend itself to a bright line test. *Weinberger*, 457 A.2d at 711. To assist in the analysis, the Delaware courts have identified two aspects of fairness for consideration: fair dealing and fair price. Fair dealing involves the transaction's timing and structure, as well as how the transaction was initiated, negotiated and approved. Fair price focuses on the economic and financial considerations surrounding the transaction. While it is important to account for both aspects of fairness, ultimately the transaction must be viewed as a whole. *Id.* The essence of the test is whether the transaction carries the earmarks of an arm's length bargain and,

if not, equity must set it aside. *Pepper v. Litton*, 308 U.S. 295, 306-07, 60 S. Ct. 238, 245 (1939).

Turning to fair dealing, the evidence at trial demonstrates that Tramiel operated in a fair manner when he purchased the portfolio from JTS. Several factors support this conclusion. First, Tramiel has demonstrated that JTS initiated and set the tone of the deal. I am not persuaded by the trustee's argument that Tramiel took advantage of JTS by asking to buy the property when he knew JTS was desperate for cash. Although Tramiel was chairman of Atari, the owner of the property for several years prior to the merger, Tramiel never tried to buy the property from Atari. Further, due to the property's strong income stream, Tramiel counseled JTS to keep the property, unless the company was desperate for cash. These pieces of evidence indicate that Tramiel had no real desire to own the property, or to take advantage of JTS to obtain it. Instead, Walker approached Tramiel, advised him that the company needed money right away and asked if he was interested in buying the portofolio. While Tramiel responded with a take it or leave it offer of $10 million, the totality of the circumstances do not suggest that Tramiel was trying to take advantage of JTS. Rather, Tramiel was trying to help. As he testified, he determined the terms on which he was willing to help JTS out of its immediate cash shortage. Moreover, as a safety precaution, he gave JTS a repurchase option because he hoped JTS would ultimately find a better deal.

Although the trustee believes that structuring the transaction as sale rather than a secured loan was an attempt to take advantage of JTS and avoid usury laws, no evidence supports that belief. Instead,

Tramiel credibly established that he told the JTS board to avoid selling the properties. However, once JTS approached him with the sale, he offered terms that would protect his own return on investment while also giving the company a twelve month window to find a better deal. This is not a situation where Tramiel put his own interests ahead of JTS's interests. Rather, he offered a deal that would provide immediate relief to JTS without exposing his own investments to significant risk, while at the same time allowing JTS to benefit from the possibility of future appreciation in the property's value.

Another factor demonstrating fair dealing is that Tramiel removed himself from all board discussions of the real estate deal and abstained from all votes concerning the sale. Thus, he made no attempt to persuade or mislead the board into accepting his offer. The trustee's evidence does not convince me otherwise. The trustee urges that Tramiel violated his duty of candor by failing to tell the other directors that the value of the portfolio of property ranged between $14 and $16 million. Although an early 1996 marketing piece by Marcus and Millichap proposed listing the individual properties at prices that aggregated between $14-16 million, there is no evidence that Tramiel was aware of this proposal at the time he bought the properties. Further, the marketing piece was not an appraisal. Tramiel testified that, at the time of the sale, he was not aware of any appraisal showing that the portfolio was worth more than $10 million.

It is also significant that the board was free to investigate the value of the portfolio of property and determine whether the price was fair. Nothing

prevented the board from obtaining value information, and evidence at trial established that JTS management and the attorneys representing JTS had access to the Marcus & Millichap marketing piece, as well as other documents that were consistent with the Marcus & Millichap marketing proposal. Testimony establishes that Tramiel advised the board that they should obtain an independent valuation and that the board knew, or at least assumed, that they might have received a better price under other circumstances. In light of JTS's need for cash, however, the board was pleased with Tramiel's offer. Under all of these circumstances, Tramiel did not act unfairly by failing to advise the board that the properties might be worth more than $10 million.

Finally, the disinterested directors' approval of the real estate transaction provides evidence of fair dealing. Although a formal board resolution signed by the disinterested directors would have been ideal, based on the evidence before me, I cannot conclude that the absence of a resolution amounts to unfair dealing. The minutes of the June 18, 1996 board meeting and the testimony of JTS's former directors provide sufficient proof that the board fully considered the real estate transaction with Tramiel and that the board was sensitive to the need for fairness. This was a sophisticated and busy board of directors that made informed decisions and relied on management and counsel to properly implement their instructions. The minutes from June 18, 1996 expressly state that the board authorized Walker and Manoliu to implement the real estate sale. While the board may have failed to comply with corporate formality by not passing a resolution, taken with the other evidence, that

technical failure is not sufficient to amount to unfair dealing.

Turning to the second prong of the fairness analysis, I also conclude that the terms of the sale, while not offering the approximate equivalent of full fair market value, offered a fair price under the circumstances existing at the time of the sale. JTS needed cash fast and, as a result, did not expect to receive the best price for the properties. Additionally, as attorney Pope testified, JTS received the benefit of some unusual sale terms because Tramiel was willing to complete the transaction without inspections or contingencies for title defects or financing. JTS also avoided the expensive brokerage fees that it otherwise would have incurred. Significantly, there is no evidence suggesting that any alternative buyer would have offered more. To the contrary, the one third party presented with the opportunity to purchase the portfolio on the same terms as Tramiel declined to go forward.

Moreover, Tramiel gave the company an option to repurchase the property, which protected JTS from any potential deficiency in price. Because the judgment of fairness must be made at the time of the transaction, it makes no difference that the option eventually expired without being exercised. In September 1996, JTS received the benefit of the option's protection. Nothing prevented JTS from conducting further investigation into the value of the properties to determine if it should exercise the option. Judged in light of all the facts, the presence of the repurchase option provides further proof that the terms that Tramiel offered were fair to JTS.

That JTS might have been able to borrow against the properties to produce a net income stream does not convince me that the terms of the sale were less than fair. Relying on *Oberly v. Kirby*, 592 A.2d 445 (Del. 1991), the trustee urges that the best way to judge fair price is to compare the price paid with the price that is likely to be available in alternative transactions. *Id.* at 471. In *Oberly*, a charitable corporation engaged in an interested transaction when it sold a large block of stock. In concluding that the sales price was fair, the court considered whether alternative buyers would have offered more. That same comparison between two interchangeable buyers is not present here. Instead, the trustee compares a secured borrowing against a sale outright. Evidence at trial, however, indicates that non-economic factors affected the choice between these two different types of transactions. For example, JTS had no use for the real property, it had a strong need to convert physical assets into cash to fund production and, if it retained the properties, valuable manpower would have been diverted to manage the properties. The alternative of borrowing does not contradict my conclusion that the sales price was fair as analyzed from the perspective of Delaware's trust fund doctrine.

As a final matter, the trustee asserts that Tramiel breached his fiduciary duty when he turned down JTS's last minute request to extend the option period. I do not agree. Tramiel dealt fairly in providing JTS with a repurchase option that would allow JTS to realize the portfolio's full value. Nevertheless, JTS made no effort to market the properties until shortly before the option was to expire. Although Eugene Hill, who was in charge of the marketing efforts, located two entities that indicated some interest in one or two

of the properties, he conceded that he had no real offer in hand for any portion of the portfolio when he requested an extension of the option. Under these facts, Tramiel did not usurp a corporate opportunity by refusing to extend the option. There was no real corporate opportunity at hand.

The evidence before me establishes that the real estate transaction carries sufficient earmarks of an arm's length bargain and, as a whole, was fair to JTS. In light of this fairness determination, the trustee's citation to *Cantor v. Perelman*, 414 F.3d 430 (3d Cir. 2005), does not change the outcome. Tramiel did not breach his fiduciary duties to JTS when he purchased the portfolio of real property from JTS.

C. The Real Property Transaction Did Not Violate California's Unfair Competition Law.

California law prohibits the use of any business practice that is "unlawful, unfair or fraudulent." Calif. Bus. and Prof. Code §17200. *Bank of the West v. Superior Court*, 2 Cal. 4th 1254, 1266-67 (1992). The definition of unfairness in a case that does not involve a competitor is whether the defendant's conduct offends established public policy or is immoral, unethical, oppressive or unscrupulous. *Smith v. State Farm Mutual Automobile Insur. Co.*, 93 Cal. App. 4th 700, 718-19 (2001). As discussed in detail with respect to the trustee's breach of fiduciary duty claims, the evidence does not support any finding that Tramiel acted unscrupulously when he purchased the real properties from JTS. Rather, as DeLeage testified, Tramiel's conduct was above board. Contrary to the trustee's argument, the evidence does not demonstrate

that Tramiel withheld knowledge of the properties' value. Tramiel testified that, at the time he bought the portfolio, he was unaware of any appraisal valuing the properties at more than $10 million. Further, JTS itself had access to the marketing information that suggested that the aggregate value of the individual properties might be significantly higher than the $10 million book value. Finally, Tramiel's refusal to extend the option period does not amount to unfairness within the meaning of § 17200 because there was no serious offer on the table. Tramiel could not be expected to extend the option indefinitely.

For these reasons, Tramiel is entitled to judgment in his favor on the trustee's claim under the California Business and Professions Code § 17200.

III. The Debt Relief Transaction.

A. JTS Did Not Repurchase its Stock in Violation of 8 Del. C. § 160 When it Forgave Mitchell's and Tandon's Promissory Notes.

Under Delaware general corporation law, a corporation may not purchase or redeem its own shares of capital stock while its capital is impaired or if the purchase would result in an impairment of the corporation's capital. 8 Del. C. §160(a). If a corporation violates § 160, each director at the time of the violation shall be jointly and severally liable for the full amount paid to purchase or redeem the stock. *Id.* at § 174. The trustee asserts that JTS violated § 160 when it provided debt relief to Mitchell and Tandon by cancelling $2.4 million in notes to the corporation in exchange for the return of their JTS stock. To succeed on this claim, the trustee must establish two elements:

1) that JTS bought or redeemed its own stock for cash or other property, and 2) that the purchase took place while JTS's capital was impaired. Because JTS was insolvent at the time the loans were cancelled, the only issue before me is whether the debt relief transaction constituted a purchase of Mitchell and Tandon's JTS stock.

The term "purchase" as used in § 160 is to be given its normal meaning. *In re Kettle Fried Chicken of America, Inc.*, 513 F.2d 807, 810 (6th Cir. 1975). In general, the Delaware courts have interpreted the term broadly to include any transaction where the corporation's clear intent was to reacquire its own shares. *See e.g., id.; Pereira v. Cogan (In re Pereira)*, 294 B.R. 449, 543 (S.D.N.Y. 2003)(insolvent corporation used controlling shareholder as intermediary to purchase stock using funds borrowed from the corporation). Applying these standards to the facts established at trial, I conclude that JTS did not repurchase stock from Mitchell or Tandon within the meaning of § 160. The clear difference with the *Pereira* case cited by the trustee is the intent behind the transaction. Here, the weight of the evidence does not establish that JTS wanted or intended to reacquire its stock. Rather, JTS wanted to ensure the continued services of two key executives during a crucial re-tooling of the company. As an incentive, the board approved the cancellation of Mitchell's and Tandon's promissory notes, leaving the details of structuring the transaction to its able legal counsel. Ultimately counsel determined that repurchasing Mitchell's and Tandon's JTS shares was problematic and structured the transaction as compensation for Mitchell's and Tandon's continued services. This structure was

entirely consistent with the board's original intent behind cancelling the notes.

The fact that Tandon may have decided to return his stock certificates to JTS does not compel a different conclusion regarding JTS's intent. The evidence before me does not support a finding that JTS ever repurchased or intended to repurchase its shares.

B. Tramiel Did Not Breach His Fiduciary Duty to JTS When He Approved the Debt Relief Transaction.

Following the proof offered at trial and the trustee's waiver of her claims that Tramiel either conspired with Mitchell and Tandon or aided and abetted them in their breach of fiduciary duties, the parties dispute whether Tramiel can assert that his approval of the debt relief transaction is subject to the business judgment rule or whether a fairness analysis must be conducted. Procedurally, the trustee argues that Tramiel is precluded from relying on the business judgment rule because he did not preserve the issue in the Final Pretrial Order.

Pretrial orders are crucial to securing a just, speedy and inexpensive determination of issues remaining for trial. *United States v. First National Bank of Circle*, 652 F.2d 882, 886 (9th Cir. 1981). Nevertheless, they must also be liberally construed to permit evidence and theories at trial that can fairly be said to be embraced within their language. *Id.* Upon careful review of the Final Pretrial Order herein, I conclude that, construing it liberally, the potential application of the business judgment rule is embraced within its language. One of the disputed legal issues set forth in

the order is whether JTS should indemnify Tramiel with respect to the allegations against him. As the trustee pointed out, such indemnity would only come into play if there was no breach of the duty of loyalty. If there was no breach of loyalty, Tramiel's individual conduct would be protected by the business judgment rule. That Tramiel understood the Final Pretrial Order to embrace the application of the business judgment rule is confirmed by his Trial Brief, which explicitly argues that Tramiel's conduct with respect to the debt relief transaction might be protected by the business judgment rule. This brief was served on trustee's counsel prior to the start of trial.

The business judgment rule, which is designed to protect managerial decisions of corporate officers and directors, presumes that the officers and directors have acted in good faith and in the best interests of the corporation. *Cede & Co. v. Technicolor, Inc.*, 634 A.2d 345, 361 (Del. 1993). If the party challenging a managerial decision rebuts the presumption, it does not create liability per se on the part of the officers or directors. Rather, it shifts the burden to the director to prove that the transaction was entirely fair to the corporation. *Pereira*, 294 B.R. at 526. The presumption created by the business judgment rule may be rebutted in two ways. First, as discussed above with respect to the real properties transaction, a fairness analysis applies where the defendant is involved in a self-dealing transaction. Second, the presumption can be rebutted when the plaintiff shows that the directors, in reaching their challenged decision, otherwise breached any one of a trio of fiduciary duties: good faith, loyalty or due care. *Cede*, 634 A.2d at 361. Here, there is no dispute that Tramiel was a disinterested director with respect to the debt relief

transaction. The question, then, is whether Tramiel breached his fiduciary duty of loyalty to JTS when he approved the concept of debt relief and left the decision regarding the structure of the transaction in Cooley Godward's hands.

Delaware defines a director's duty of loyalty in broad and unyielding terms. *Pereira*, 294 B.R. at 527. It requires that the best interest of the corporation and its constituent groups take precedence over any interest not shared by those constituent groups. Importantly, here, the Delaware Supreme Court has recognized that an abdication of directorial duties can constitute a beach of the duty of loyalty. *Id.* at 528, *citing*, *Lutz v, Boas*, 171 A.2d 381, 395-96 (1961).

Relying on *Pereira*, the trustee asserts that Tramiel is not entitled to assert the business judgment rule defense because he effectively abandoned his duty to investigate, evaluate and supervise the debt relief, a transaction that involved other interested directors. The evidence, according to the trustee, establishes, at best, that Tramiel and his fellow directors delegated their supervisory role to Cooley Godward and ignored their duty to evaluate and ratify the details of the transaction once they approved the concept of debt relief. I do not agree with the trustee's assessment of the evidence.

The evidence shows that Tramiel and Johnson, as a quorum of the board, were presented with a proposal to forgive Mitchell's and Tandon's indebtedness to JTS. Both Tramiel and Johnson were sure that debt relief was essential to keep Mitchell and Tandon operating the company. They knew the amount of the proposed debt relief and considered it a small price to ensure the

continued employment of Mitchell and Tandon. This is far different from the circumstances in *Pereira*, where the board ratified a director's past compensation without even knowing what level of compensation it was ratifying. Although there is no evidence here that the JTS board considered studies comparing the amount of the proposed debt relief to the salaries of similarly situated executives, a board is not required to obtain expert advice. *Chesapeake Corp. v. Shore*, 771 A.2d 293, 331 (Del. Ch. 2000)(no legal requirement that a board consult advisors as long as the board has adequate information to make an informed judgment). Significantly, neither Tramiel nor Johnson was new to the world of executive compensation. Both had served on multiple boards of directors. It is entirely reasonable to infer from the evidence that they drew on that body of knowledge and experience in reaching their decision that the debt relief was in JTS's best interest.

Having determined that Tramiel did not breach his fiduciary duty of loyalty, the business judgment rule applies to shield Tramiel from liability for the decision to forgive Mitchell's and Tandon's indebtedness to JTS. It is presumed that Tramiel acted in good faith and in the best interests of the corporation. *Cede & Co. v. Technicolor, Inc.*, 634 A.2d 345, 361 (S. Ct. Del. 1993). I see no evidence to the contrary.

III. The NationsBanc and Series D/E Transaction

A. The Series D/E Stock Exchange Was Not A Repurchase of Stock Within the Meaning of 8 Del. C. § 160.

As discussed above with respect to the debt relief transaction, no corporation may "purchase or redeem its own shares of capital stock for cash or other property" while its capital is impaired or if the redemption would result in an impairment of the corporation's capital. 8 Del. C. § 160(a). The statute was enacted to prevent boards from draining a corporation's existing assets to the detriment of creditors and the corporation's long-term health. *Klang v. Smith's Food & Drug Centers, Inc.*, 702 A.2d 150, 154 (Del. 1997). Based on the evidence before me, I am not persuaded that JTS violated this section when it replaced the Series D preferred stock with the newly issued Series E preferred shares. Although the Delaware courts have generally given § 160 a broad interpretation, the statute contains an explicit limitation that I cannot ignore. To violate § 160, a corporation must purchase or redeem its shares "for cash or other property." Here, the evidence establishes that JTS issued new shares of stock to replace the Series D preferred stock. No cash was involved in the transaction. Additionally, no property of JTS was transferred when the Series E stock was issued in exchange for the Series D shares. "[A] share of capital stock represents a unit of ownership interest and has no extrinsic value to the corporation itself." *In re Curry and Sorensen, Inc.*, 57 B.R. 824, 829 (9th Cir. B.A.P. 1986). Agreeing with that proposition, the ninth circuit has similarly held that the issuance of a corporate

debtor's stock is not a transfer of an interest of the debtor in property. *Decker v. Advantage Fund, Ltd.*, 362 F.3d 593, 596 (9th Cir. 2002)(affirming the dismissal of fraudulent conveyance claims based on the issuance of stock)

The trustee's assertion that JTS also gave a blanket lien on all of its assets in consideration for the reacquisition of the Series D stock is not borne out by the evidence. According to the documentation referenced by the trustee, JTS provided the blanket lien to NationsBanc as security for NationsBanc's $10 million credit facility, not in exchange for the Series D stock. While testimony at trial established that JTS provided Amber and the director participants with a second priority blanket lien, that junior lien was consideration for the investors' willingness to release $10 million from escrow to be used as a guarantee for the NationsBanc credit facility. Again, it was not property that JTS gave in exchange for the Series D stock. Indeed the exchange of Series D and Series E stock was completed in December 1997, more than a month before JTS allowed the lien against its assets.

Because JTS simply repriced its own equity, it did not repurchase its shares for cash or other property within the meaning of 8 Del. C. § 160. Judgment will be entered in Tramiel's favor on this claim.

B. Tramiel Did Not Breach His Fiduciary Duty to JTS With Respect to the Series D/E Stock Transaction

Because the guarantee of the NationsBanc line of credit resulted in an exchange of the Series E stock for Series D stock and ultimately provided Tramiel, as one

of the director participants, with an interest in a second priority blanket lien against JTS's assets, it constitutes a self-interested transaction. As a result, Tramiel has the burden of establishing its fairness to JTS. Based on the evidence before me and applying the standards discussed above, I conclude that, when taken as a whole, the Series D/E stock exchange bears sufficient characteristics of fairness to allow it to withstand careful scrutiny.

At the time of the Series D/E stock exchange, JTS was on a positive swing in its business but needed more money to fund its operations if it was going to turn the corner. Amber was unwilling to release more cash from the escrow because JTS's Series D preferred stock had become virtually worthless and provided insufficient consideration. JTS was actively looking for other sources of funds. NationsBanc, an independent financial institution, was willing to lend money, but as is common with a distressed company, the bank wanted collateral security. Ms. Martinson's notes from early December 1997 reflect that Amber was willing to put up $10 million as security if JTS was willing to re-price its Series D stock in consideration for Amber's agreement to release an additional $10 million from the cash escrow account.

With respect to Tramiel's involvement, the D/E stock exchange involved fair dealing. Martinson testified that the terms of the NationsBanc - Series D/E stock transaction were negotiated at arms length between counsel for JTS and counsel for Amber. It is significant that, by December 1997, Tramiel did not have any ability to use his insider position to control the transaction to his own advantage or to the disadvantage of other creditors. Tramiel and the other

directors who had placed funds in the cash escrow had given Amber sole authority over the cash escrow account well before the NationsBanc - Series D/E Stock transaction came under consideration. Additionally, as an interested director, Tramiel did not participate in board discussions regarding the NationsBanc transaction. He understood that the transaction was between Amber and the company. After September 1997, when he placed $3 million in the cash escrow, he was just along for the ride.

Further, contrary to the trustee's belief, there is no evidence that the director participants used their directorial powers to force JTS to intentionally hinder creditors by requiring a blanket lien for NationsBanc. Both Tramiel and Tandon testified that, because of their interest, they simply did not participate as part of the board with respect to the NationsBanc transaction. Moreover, Ms. Martinson's notes reveal that it was JTS management who was looking for a way to put a senior security interest into place.

Another factor suggesting fair dealing is that the structure of the transaction was not unusual or inappropriate under the circumstances. Although JTS agreed to both reprise the D/E stock and authorize a second priority blanket lien in exchange for the use of the escrowed funds, JTS was a seriously distressed company. Other sources of funds were non-existent. The fact that other lenders were not willing to lend JTS money suggests that extraordinary protection was required.

Turning to the fair price aspect of the transaction, the weight of the evidence establishes that the exchange of the Series D and Series E preferred stock

involved a fair price. On this issue, both sides provided expert testimony, but Tramiel's expert, Scott Hakala, was more convincing and his testimony is accorded substantial weight. Dr. Hakala explained that the binomial model and the Black-Scholes model, on which the trustee's expert relied, tended to overvalue stock options in a distressed company where there was a significant risk that the stock option might be worth nothing. Instead, Dr. Hakala, considered various probabilities involving the future value of JTS's stock to determine the potential benefit that Amber and the director participants received by exchanging the Series D stock for the Series E stock. Using his formula, Dr. Hakala estimated that with respect to shares of preferred stock out of escrow, the Series E shares were worth approximately $ 4 million more than the Series D shares. He also insisted, however, that this raw value should be discounted because the Series E shares were not immediately marketable.

Next, Dr. Hakala testified that the Series D/E exchange also had value to JTS because the company received immediate access to $10 million that enabled the company to continue operating at a time when it was starting to gain traction in the industry. Dr. Hakala testified that from JTS's perspective in December 1997, the immediate access to funds resulted in $20 - $40 million in value created by allowing the company to produce more product that could then be sold at a profit in a positive market. Based on this evidence, JTS received a potential benefit between $20 and $40 million in return for the newly issued Series E stock that had value to the recipients, but no intrinsic value to the company itself. What JTS relinquished was the right to receive the higher conversion price attached to the Series D

shares, a speculative right at best because the Series D shares were deep out of the money and conversion was unlikely. Under these circumstances, the weight of the evidence demonstrates that the Series D/E stock transaction involved a fair price.

Finally, the eventual placement of a blanket lien against JTS's assets does not make the Series D/E stock transaction unfair. First, JTS wanted the blanket lien for reasons unrelated to the release of escorted funds to guarantee the NationsBanc credit facility. Second, even though JTS's financial statements valued its assets at $46 million around the time of the NationsBanc transaction, Dr. Hakala testified that only the liquidation value of those assets provided security under the blanket lien. According to Hakala, the liquidation value of JTS's assets was "maybe $10 million in security value." Since the security value of the assets was borderline at best, it is not surprising that in the first instance Amber requested the Series D/E stock exchange as consideration for its guarantee.

With respect to Tramiel, the NationsBanc-Serie D/E transaction involved both fair dealing and fair price, and Tramiel has satisfied his burden of establishing the transaction's fairness. As a result, Tramiel's participation in the transaction did not breach his fiduciary duty to JTS.

C. The Trustee Has Established that the Blanket Lien that JTS Gave to Amber, Tramiel, Tandon and Mitchell Is An Actual Fraudulent Conveyance.

Section 548 of the Bankruptcy Code allows a trustee to avoid transfers of a debtor's property made within one year of filing bankruptcy if the debtor made the transfer with actual intent to hinder, delay, or defraud any creditor. 11 U.S.C. § 548(a)(1). The focus of this provision is on the state of mind of the debtor, not the transferee. *In re Cohen*, 199 B.R. 709, 716-17 (9th Cir. B.A.P. 1996). Further, consideration provided for a transfer is not material. Even a market price transaction may qualify as actually fraudulent if the debtor has the requisite state of mind to hinder, delay or defraud a creditor. *Id.* at 717. *See also Tavenner v. Smoot*, 257 F.3d 401, 407 (4th Cir. 2001)(nothing in § 548 requires showing that a fraudulent conveyance actually harmed a creditor). Because the statutory language is disjunctive, intent to defraud is not required; it is enough that the debtor intends to hinder or delay a creditor. *In re Bernard*, 96 F.3d 1279, 1281 (9th Cir. 1996)(interpreting same statutory standard found in 11 U.S.C. §727(a)(2)). Finally, there is no requirement that the debtor intend to hinder all of its creditors because the statute penalizes transfers with intent to hinder, delay, or defraud "any creditor." *See In re Adeeb*, 787 F.2d 1339, 1343 (9th Cir. 1986)(interpreting § 727(a)(2)).

To prevail on her actual fraudulent conveyance claim, the trustee must prove the requisite intent to hinder delay or defraud creditors by a preponderance of the evidence. Either direct proof or circumstantial evidence, referred to as "badges of fraud," can be

sufficient. Here, the trustee points to direct evidence of JTS's intent. Pamela Martinson, a Cooley Godward attorney, testified that in early November 1997, JTS was looking for a way to put a senior secured interest in place as a means to protect itself against the claims of unpaid trade vendors who were trying to attach JTS's assets. Even though the stipulated facts in the Final Pretrial Order establish that NationsBanc was willing to provide its $10 million line of credit with JTS's accounts receivable and intangibles serving as security, Martinson's notes show that Prezioso specifically asked her to make sure that all of JTS's assets were put up as collateral. Similarly, JTS gave Amber, Mitchell, Tandon and Tramiel a second priority blanket lien to the extent that their certificates of deposit that guaranteed the NationsBanc loan were drawn down. Even though this kind of senior security interest is a typical way to maintain order among creditors for the benefit of all creditors, under the standards discussed above, protecting assets from some creditors for benefit all creditors still amounts to hindrance or delay within the meaning of §548(a)(1). *See Adeeb*, 787 F.2d at 1343, *citing*, *Matter of Trinity Baptist Church*, 25 B.R. 529, 532-33 (Bankr. M.D. Fla.1982). Because the preponderance of the evidence establishes that JTS gave blanket liens with intent to hinder and delay creditors, Tramiel's interest in the blanket lien is avoidable under § 548(a)(1).

D. Tramiel is Not Indirectly Liable for Acts of Other Fiduciaries With Respect to the NationsBanc - Series D/E Transaction.

The trustee has asserted that Tramiel should be indirectly liable for NationsBanc - Series D/E stock

transaction because Tramiel either aided and abetted Amber, Mitchell and Tandon or participated in a joint venture with them. The trustee, however, offered no evidence of any breach of fiduciary duty separate from the evidence she offered against Tramiel. As a result, the indirect liability claims must rise or fall with the claim for breach of fiduciary duty asserted directly against Tramiel. Because the evidence established that the NationsBanc - Series D/E Transaction was entirely fair in as far as Tramiel's dealings with JTS, the trustee's claims for indirect liability also fail.

E. The Trustee's Claims for Subordination of Tramiel's Lien Are Moot.

In light of the above finding that JTS put Tramiel's lien interest in place with actual intent to hinder or delay creditors, it is unnecessary to consider whether § 510 of the Bankruptcy Code also requires subordination of the lien. Because Tramiel's lien against JTS's assets is voidable as a fraudulent conveyance, the trustee's lien subordination claims are moot.

IV. The Trustee's Recovery On Her Fraudulent Conveyance Claims Is Not Affected By Any Asserted Right to Indemnity, Offset or Settlement Credits.

The trustee prevailed on her two fraudulent conveyance claims against Tramiel. As the ninth circuit has recognized, recovery of a fraudulent conveyance cannot be offset against or exchanged for a general unsecured claim. *Acequia, Inc. v. Clinton (In re Acequia, Inc.)*, 34 F.3d 800, 817 (9th Cir. 1994); *United Energy*, 944 F.2d at 597. As a result, any claim

that Tramiel may assert against the estate for indemnity or otherwise cannot be used to offset his obligation to return the excess value that he received in connection with the real properties transaction. This makes sense because allowing offsets would thwart the very purpose of the fraudulent transfer laws. *Acequia*, 34 F.3d at 817; *Bustamante v. Johnson (In re McConnell)*,, 934 F.2d 662, 667 (5th Cir. 1991). Tramiel must return the excess value to the estate and wait to recover on any allowed claim along with the other unsecured creditors.

Additionally, the amounts paid by former defendants in settlement of the trustee's claims against them do not reduce Tramiel's liability with respect to the real properties transaction. The claim on which the trustee prevailed was premised on the California fraudulent transfer laws. Federal courts will apply state court settlement procedures in determining the manner in which a co-defendant's settlement will set off a non-settling defendant's liability. *Slaven v. BP America, Inc.*, 958 F. Supp. 1472, 1477-78 (C. D. Cal. 1997). Under California law, a good faith settlement in a tort action entitles the non-settling defendant to a settlement credit equal to the settlement amount paid by settling defendants who are claimed to be liable for the same tort. Cal. Code Civ. Pro. § 877. In this case, however, Tramiel was the only defendant named in the trustee's claim that the real properties transaction constituted a constructive fraudulent transfer. As a result, with respect to the claim on which the trustee has recovered, there were no settling co-defendants and § 877 is inapplicable.

With respect to the avoidance of the NationsBanc Lien, the trustee only seeks return of Tramiel's interest in the lien. She has expressly waived any recovery against Tramiel for the value of the entire NationsBanc lien. As a result, Tramiel is not entitled to a credit to the extent that the other NationsBanc guarantors have already assigned their lien interests to the estate.

V. The Trustee Is Entitled to Prejudgment Interest on Her Recovery of the Excess Value Transferred in Connection With the Real Properties Transaction.

The ninth circuit has recognized that state law regarding prejudgment interest is applicable to avoidance actions under § 544(b). *Acequia, Inc. v. Clinton (In re Acequia)*, 34 F.3d 800, 818 n.4 (9th Cir. 1994); *Hayes v. Palm Seedlings Partners (In re Agrigultural Research and Technology Group, Inc.)*, 916 F.2d 528, 541 (9th Cir. 1990). Tramiel argues that, under California law, awards of prejudgment interest are discretionary, and no interest is appropriate under the circumstances of this case. The trustee, on the other hand, asserts that prejudgment interest should be awarded from the time of the transaction, September 1996, forward. I do not agree with either party.

Prejudgment interest is an essential part of making the debtor's estate whole from the loss of the property transferred to Tramiel. However, an award from September 1996 is in appropriate because the real estate sale was constructively fraudulent and there is no evidence of actual fraud or culpable misconduct that occurred at the time of the transfer. The most

equitable result is to award interest, but only from the date that the trustee filed her adversary proceeding against Tramiel. *See, e.g., Nelson Co. v. Amquip Corp. (In re Nelson Co.)*, 117 B.R. 813, 818 (Bankr. E.D. Pa. 1990), *aff'd*, 128 B.R. 930 (E.D. Pa. 1991)(prejudgment interest allowed from the date of demand for return of preferential transfer or, if no demand, from the filing of the adversary proceeding).

Tramiel has not disputed that the appropriate rate of interest under California law is the constitutional rate of seven percent. *See* Cal. Const. art. XV, § 1. The trustee is entitled to receive prejudgment interest, at the rate of seven percent (7%), from the date that the trustee filed this adversary proceeding, November 16, 2000.

CONCLUSION

For the reasons set forth above, the trustee is entitled to recover $1,387,185 as a constructive fraudulent conveyance pursuant to § 544 of the Bankruptcy Code and California fraudulent conveyance laws. This recovery will be subject to an award of prejudgment interest at the rate of 7% measured from the filing of this adversary proceeding. Additionally, as part of the NationsBanc transaction, JTS placed a blanket lien on its assets in an attempt to hinder, delay or defraud its creditors. Tramiel's interest in the lien against JTS's assets is avoided as an actual fraudulent conveyance pursuant to § 548 of the Bankruptcy Code. In all other respects, Tramiel is entitled to judgment in his favor on the trustee's claims.

The parties are directed to confer and submit a proposed judgment that is consistent with this opinion.

* * *

[*Service List omitted in printing of this appendix*]

* * *

APPENDIX F

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Suzanne L. Decker, Trustee

UNITED STATES BANKRUPTCY COURT
NORTHERN DISTRICT OF CALIFORNIA
SAN JOSE DIVISION

Case No. 98-59752 MM
Chapter 7

A.P. NO. 00-5423

[Filed April 23, 2004]

In Re	)
	)
JTS CORPORATION,	)
	)
Debtor.	)
	)
SUZANNE L. DECKER, TRUSTEE,	)
	)
Plaintiff,	)

vs.

ROGER W. JOHNSON, LIP-BU TAN, JEAN D. DeLEAGE, DAVID T. MITCHELL, JACK TRAMIEL, SIRJANG LAL "JUGI" TANDON, AMBER ARBITRAGE LDC, a private investment fund incorporated in the Cayman Islands, COOLEY GODWARD, LLP, MATTHEW W. SONSINI, ANDREI M. MANOLIU, ANNA B. POPE,

Defendants.

ORDER APPROVING GOOD FAITH SETTLEMENT

Date: April 23, 2004
Time: 11:30 a.m.
Place: 280 So. First St., Rm. 3070
San Jose, CA

Suzanne L. Decker ("Plaintiff"), the trustee of the bankruptcy estate of JTS Corporation ("Debtor") and the plaintiff in the adversary proceeding referred to above, came on regularly for hearing at the above date, time, and place. Appearances were as noted on the record. Having reviewed all papers and considered counsels' arguments; and for good cause shown,

THE COURT MAKES THE FOLLOWING FINDINGS:

1. The Plaintiff filed a Second Amended Complaint ("Complaint") against former directors Sirjang Lal "Jugi" Tandon ("Tandon") and David T. Mitchell ("Mitchell") (collectively the "Settling Directors"); former director Jack Tramiel ("Tramiel"); former directors Roger Johnson, Lip Bu Tan and Jean DeLeage (collectively the "Dismissed Defendants"); Amber Arbitrage LDC ("Amber"); the Debtor's former counsel, Cooley, Godward, LLP ("Cooley"), Matthew W. Sonsini ("Sonsini"), Andrei M. Manoliu ("Manoliu"), and Anna B. Pope ("Pope") (collectively, the "Attorney Defendants").

2. The Complaint contained claims for relief for breach of fiduciary duty, fraudulent conveyance, equitable subordination, illegal redemption of shares, and other claims for relief arising out of five distinct business transactions.

3. This Court reviewed and considered lengthy motions for dismissal.

4. This Court reviewed and considered lengthy motions and cross-motions for summary adjudication, including detailed declarations containing the parties assertions and contrary assertions of fact related to the specified transactions that were the basis for the Complaint.

5. On September 30, 2003, this Court entered a 36-page opinion on cross summary judgment motions, which opinion clarifies and identifies in great detail

the Court's analysis of the claims, the legal issues, and the factual issues to be decided at trial.

6. After two separate mediations before the Honorable Coleman Fannin of Judicial Arbitration and Mediation Service and a mediator's demand, the Plaintiff and the Settling Defendants agreed to settle the dispute on the basis set forth in the Settlement Agreement ("Settlement Agreement"), a copy of which is attached hereto as **Exhibit A**.

7. The Settlement Agreement calls for the Settling Defendants to pay the estate the aggregate sum of $4,500,000 ("Settlement Sum") as follows: the Attorney Defendants will pay $3,075,000, Mitchell shall pay $600,000, and Tandon shall pay $825,000. Additionally, the Settlement Agreement allows for the Mitchell's and Tandon's interest in any liens against the estate related to the NationsBanc-Series D/E exchange to be avoided and preserved for the estate's benefit.

8. The Settlement Agreement is conditioned upon the Court entering an order relieving the Settling Defendants from any liability for indemnity or contribution in favor of any other person, including, without limitation, the remaining defendant Tramiel and the Dismissed Defendants.

9. The Settlement Agreement was entered into in good faith and allows for payments by the Settling Parties that are within the reasonable range of their proportional share of comparative liability owed to the Plaintiff, and that are not grossly disproportionate to the Settling Defendants' liability.

10. This Court has considered Plaintiff's Motion to Approve Good Faith Settlement, and has approved the compromise of controversy between the Plaintiff and the Dismissed Defendants.

IT IS HEREBY ORDERED AS FOLLOWS:

1. The Settlement Agreement [*handwritten insertion by Judge Morgan:* **except for the last sentence of paragraph 8**] is approved as a good faith settlement and bars Tramiel and the Dismissed Defendants from seeking contribution and/or indemnity from the Settling Defendants pursuant to CCP §877 and federal common law.

2. This Court reserves its right to allocate culpability amongst all of the Defendants upon Tramiel's request for a credit for the amounts paid by the Settling Defendants if, after a trial, this Court determines that Tramiel is liable as joint tortfeasor on any claim for relief.

Dated: APR 23 2004, 2004

MARILYN MORGAN
The Honorable Marilyn Morgan
United States Bankruptcy Judge

SETTLEMENT AGREEMENT, MUTUAL RELEASE AND COVENANT NOT TO SUE

This SETTLEMENT AGREEMENT, MUTUAL RELEASE, AND COVENANT NOT TO SUE (the "Agreement") is made and entered into as of the date of the last party to sign this Agreement (the "Effective Date"), by and between COOLEY GODWARD, LLP, MATTHEW W. SONSINI, ANDREI M. MANOLIU, ANNA B. POPE (the Attorney Defendants") and SIRJANG LAL (JUGI) TANDON (sued herein as Sirjong Lal Tandon) and DAVID T. MITCHELL (the "Director Defendants"), collectively referred to as the Settling Defendants, and SUZANNE DECKER ("Decker" or "Trustee") AS DULY APPOINTED TRUSTEE FOR THE JTS CORPORATION BANKRUPTCY ESTATE ("Estate"). Settling Defendants and Decker are collectively referred to as the "Parties."

RECITALS

WHEREAS, in or around November 1998, certain of JTS Corporation's ("JTS") creditors forced it into chapter 11 bankruptcy in the United States Bankruptcy Court, Northern District of California (the "Court"), San Jose Division, Case No. 98-59752 MM, which chapter 11 case later was converted into a chapter 7 bankruptcy case (the "Bankruptcy Case"); and

WHEREAS, the Settling Defendants and Decker are parties to a lawsuit, Suzanne L. Decker v. Roger Johnson, et al., Adversary No. 00-5423 (the "Action"), in which Decker has alleged claims against the Settling Defendants for fraudulent conveyances, illegal

share repurchase by JTS, breach of fiduciary duty, legal malpractice, and aiding and abetting breach of fiduciary duty arising out of certain transactions involving JTS during the time Decker alleges the Director Defendants served on the Board; and

WHEREAS, the Parties desire to settle the Action and Decker desires to release the Settling Defendants from any and all liability concerning or arising out of the Action and seeks the Court's order that such a settlement is fair and reasonable and precludes any claims against Settling Defendants for contribution or indemnity.

NOW, THEREFORE, in consideration of mutual agreements, promises, covenants, and other good and valuable consideration set forth herein, it is hereby agreed by and between the Parties as follows:

AGREEMENT

1. Obligations.

1.1 In full settlement and compromise of any and all claims the Parties may have against each other related to and/or arising out of the Action, the Bankruptcy Case, and/or the Settling Defendants' relationships with JTS (collectively, "the Released Claims") Settling Defendants shall pay to Decker the total sum of Four Million Five Hundred Thousand Dollars ($4,500,000) (the "Settlement Sum"). The Settlement Sum shall be paid within five (5) days after receipt of notice of entry of the order relieving Settling Defendants from any liability for indemnity or contribution pursuant to Paragraph 1.2, below. The Settlement Sum shall be paid as follows: (1) The

Attorney Defendants shall pay $3,075,000 which the Trustee allocates to the claims of malpractice related to Series B and C and forgiveness of indebtedness. The Attorney Defendants deny that they are liable to Trustee for malpractice or any misconduct and the payment is not to be construed as an admission of any responsibility. (2) Mitchell shall pay $600,000 and Tandon shall pay $825,000, which payments the Trustee allocates to the claims related to the forgiveness of promissory notes and the repurchase of those shares with those notes. The Director Defendants, however, deny they are liable to Decker on these claims and the payments are not to be construed as an admission of any responsibility.

1.2 Upon the execution of this Agreement, Decker shall file a Notice of Motion and Motion to Approve Compromise (the "Motion"). The Motion shall request an order approving this Agreement and finding that the settlement is fair, reasonable, in good faith, and relieves the Settling Defendants from any liability for indemnity or contribution. This Agreement is conditioned upon the Court entering an order relieving the Settling Defendants from any liability for indemnity or contribution in favor of any other person, including, without limitation, Jack Tramiel, Roger Johnson, Jean DeLeage and/or Lip-Bu Tan (the "Good Faith Order"). Within five (5) days after receipt of Notice of Entry of the Good Faith Order, Settling Defendants shall pay the Settlement Sum by wire transfer pursuant to the wiring instructions attached hereto as Exhibit A. Within two (2) business days after receipt of the Settlement Sum, Decker shall file a Notice of Entry of Dismissal with Prejudice in the Action of the Settling Defendants.

2. Mutual and General Release of All Claims.

2.1 In consideration of the obligations and release of the Parties set forth herein and effective upon filing of a Notice of Entry of Dismissal as set forth in Paragraph 1.2, above, each of the Parties on behalf of his/her/itself and his/her/its respective representatives, agents, attorneys, predecessors, constituents, successors, and assigns, hereby fully and forever releases, acquits, and discharges each of the other Parties and each of the other Parties' respective agents, heirs, relatives, spouses, family members, executors, administrators, trustors, trustees, predecessors, successors, assigns, attorneys, officers, directors, shareholders, employees, investors, stockholders, administrators, and predecessor, successor corporations, partnerships, affiliates (which in the case of Defendant Tandon shall include, but not be limited to, Tandon Family Partnership, Lunenberg S.A., Tantec Magnetics, Inc., Tandon Associates, Tandon Corporation, Modular Electronics, Celetron, and any and all of his relatives) of and from any claims, duties, demands, causes of action, obligations, liabilities, liens, taxes, damages, losses, costs, attorneys' fees and expenses of every kind and nature whatsoever, known or unknown, suspected or unsuspected, which they may have by reason of any past act, inaction, duty, obligation, cause or thing arising out of and/or relating to the Released Claims, whether or not included in the Action.

Decker acknowledges that this release constitutes a full and complete release of, and bar to, any and all claims against the Settling Defendants by JTS, and any of its parties in interest and/or constituencies, including, without limitation, all claims that the estate

could assert on behalf of JTS' creditors and shareholders.

The Settling Defendants, acknowledge that this release fully and forever releases any and all claims or rights they may have to make a claim against, or receive any payment from, the Estate.

2.2 Notwithstanding any other provision of the Agreement, the Parties do not intend any release of claims or interests described in this Section 2 to be a release of the Director Defendants' secured claims and interests in the Estate's past, present or future property. Rather, such claims are avoided and specifically preserved for the Estate.

2.3 The Parties agree that the release set forth in this Section 2 shall be and remain in effect in all respects as a complete general release as to the matters released. The Parties specifically agree that this release does not extend to or inure to the benefit of Jack Tramiel or any party who received directly or indirectly from him property which belonged to JTS. The release shall not extend to any claims to enforce the terms of this Agreement. The Director Defendants and the Attorney Defendants also hereby release each other and their agents from any claim for contribution or indemnity related to the Action.

2.4 The Parties represent and warrant that none of the matters released that are required to be released in this Section 2 above have been sold, assigned, or transferred by them, in whole or in part, and that they are fully entitled and authorized subject to Court approval to cause all of said respective matters

released, actually to be released in full as provided in this Section 2.

2.5 This Agreement extends to claims that the Parties do not know or suspect to exist in their favor, which if known by them would have materially affected their decision to enter into this Agreement. The Parties acknowledge that they are familiar with, and hereby knowingly and voluntarily waive any and all rights and benefits conferred by Section 1542 of the California Civil Code, which reads in full as follows:

> A GENERAL RELEASE DOES NOT EXTEND TO CLAIMS WHICH THE CREDITOR DOES NOT KNOW OR SUSPECT TO EXIST IN HIS FAVOR AT THE TIME OF EXECUTING THE RELEASE, WHICH, IF KNOWN BY HIM, MUST HAVE MATERIALLY AFFECTED HIS SETTLEMENT WITH THE DEBTOR.

The Parties acknowledge and agree that this waiver is an essential and material term of this Agreement, and without such waiver, this Agreement would not be entered into. The Parties have been advised by legal counsel with respect to such waiver, and understand and acknowledge the significance and consequences of this Agreement and of this express waiver of California Civil Code §1542.

3. Covenant Not To Sue. Each of the Parties hereto covenants and agrees that such Party will not individually or with any other person in any way commence or aid in any way, except as required by the legal process, prosecute or cause or permit to be commenced or prosecuted against any of the other Parties to this Agreement any action or other

proceeding based upon any claim that is the subject of this Agreement, including but not limited to any claim arising out of, alleged in, or related to the Released Claims, save and except only any breach of this Agreement. This Agreement shall be deemed breached and a cause of action shall be deemed to have accrued immediately upon the commencement or prosecution of any other action or proceeding contrary to the provisions of this Agreement. Settling Defendants further agree not to provide any further assistance to the remaining defendant in connection with the Action.

4. Representations and Warranties.

4.1 The Parties make the representations and warranties herein with the understanding that each of the other Parties enter into this Agreement in reliance upon each of these representations and warranties, and that without these representations and warranties, none of the other Parties would enter into this Agreement.

4.2 Each of the Parties represents and warrants that they are executing this Agreement completely voluntarily, and without any duress or undue influence of any kind from any source, and that they have full power, authority, and legal right to execute, deliver, and perform all actions required under this Agreement.

4.3 Each of the Parties represents and warrants that they have been fully advised by their attorney concerning the effect and finality of this Agreement and that the Party understands, without reservation or doubt, the effect and finality of this Agreement.

Each of the Parties further represents and warrants that they desire to forever and fully release and discharge all other Parties, as set forth herein, and understands that by execution of this Agreement, no further claims against any of the other Parties arising out of the matters released herein may ever be asserted.

4.4 Each of the signatories hereto warrants and represents that he or she is competent and authorized to enter into this Agreement on behalf of the Party for whom he or she purports to sign.

5. Confidentiality.

5.1 Except for the purpose of obtaining court approval of this Agreement, or in the good faith operation of the Parties' respective businesses, or for purposes of enforcing the Agreement, or as otherwise may be required by law, none of the Parties to this Agreement will disclose any of its material terms to any person, except to their respective accountants, attorneys, financial advisors and/or partners. The Parties agree not to voluntarily publicize or discuss the Action, the conduct of the Settling Parties, or the resolution of the Action to persons who are not Parties to this agreement or their agents.

5.2 This covenant not to disclose is subject to the following exception: If any of the Parties is asked about the status or outcome of this Action or any claim potentially asserted by any other Party, that Party may reply with words to the effect of: "The matter has been resolved on mutually acceptable terms," but shall not otherwise indicate the material terms or nature of the resolution of this dispute.

5.3 None of the restrictions set forth in this Section 5 shall apply to any information that becomes public knowledge by means not in violation of the provisions of this Agreement.

6. Compromise of Disputed Claims. This Agreement is the result of good faith compromise and settlement of disputed claims. It takes into account the costs of defense and other matters. It shall never, at any time or for any purpose, be considered an admission of the correctness of the claims advanced by any of the Parties, or of any liability or responsibility by any of the Parties, each of whom continues to deny all liability, disclaim all responsibility, and dispute the factual allegations claimed by the other Parties.

7. Construction of Agreement. This Agreement is the product of negotiation and preparation by and among the Parties and their respective attorneys. Accordingly, all Parties acknowledge and agree that this Agreement shall not be deemed prepared or drafted by one party or another, or the attorneys for one party or another, and shall be construed accordingly.

8. Cooperation. The Settling Defendants who reside in California agree to accept subpoenas for trial in the Action, which can be delivered by mail to their current attorneys of record. Any service of a subpoena on Defendant Mitchell must comply with the applicable provisions of the Federal Rules of Civil Procedure and Title 28 of the United States Code. The Settling Defendants also agree that upon full compliance with Section 1, above, they will provide currently available reports upon request and to advise their expert witnesses that the Settling Defendants

have no objection to the experts being consulted by Decker's attorneys, as long as Decker pays all fees for such consultation.

9. Attorneys' Fees and Costs. The Parties acknowledge and agree that each shall bear their own costs, expenses, and attorneys' fees arising out of the Action, the negotiation, drafting, and execution of this Agreement, and all matters arising out of, or connected therewith.

10. Governing Law. This Agreement, its interpretation, performance and enforcement, and any and all matters related in any way to it, shall be interpreted in accordance with and governed in all respects by the laws of the State of California.

11. Jurisdiction and Venue. The United States Bankruptcy Court for the Northern District of California, San Jose Division shall retain exclusive jurisdiction over this Agreement and the resolution of any breach thereof.

12. Binding Effect. Once executed by all Parties, this Agreement shall be binding upon and inure to the benefit of all Parties, and their respective heirs, executors, administrators, trustors, trustees, predecessors, successors, assigns and attorneys.

13. Headings. The various headings used in this Agreement are solely for the convenience of the Parties and shall not be used to interpret this Agreement.

14. Counterparts. This Agreement may be executed in counterparts, including facsimile, each of

which shall be deemed an original, and all of which when taken together shall constitute one agreement, which shall be binding upon all Parties, notwithstanding that the signatures of the Parties do not appear on the same page.

15. Modifications. No amendment, change, or modification of this Agreement shall be valid or binding, unless it is in writing and signed by each of the Parties.

16. Entire Agreement. This Agreement constitutes the complete, final, and entire agreement among the Parties with respect to the subject matter hereof and supercedes any other prior and contemporaneous oral or written agreements, negotiations, and discussions with respect to the subject matter hereof. There are no representations, warranties, agreements, arrangements, undertakings, oral or written, between or among the Parties relating to the terms of this Agreement that are not fully expressed herein.

17. Acknowledgement. Each of the Parties to this Agreement has read the foregoing Agreement and fully understands and agrees to it.

IN WITNESS WHEREOF, the Parties to this Agreement have signed this Agreement below.

Dated: _____, 2004

_____
SUZANNE L. DECKER,
Duly Appointed Trustee for
the JTS Corporation
Bankruptcy Estate

Dated: _____, 2004

_____
Managing Partner,
COOLEY GODWARD, LLP

Dated: _____, 2004

_____
MATTHEW W. SONSINI

Dated: _____, 2004

_____
ANDREI M. MANOLIU

Dated: _____, 2004

_____
ANNA B. POPE

Dated: _____, 2004

_____
SIRJANG LAL (JUGI)
TANDON

Dated: _____, 2004

_____
DAVID T. MITCHELL

EXHIBIT A

Wire Transfer Instructions

Bank:	City National Bank 2101 Webster Street, 14th Floor Oakland, CA 94612
Telephone Number:	(510) 836-6500
Account Title:	Wendel, Rosen, Black & Dean, LLP Attorney Trust
Account Number:	444006188
ABA Number:	122016066

APPENDIX G

UNITED STATES BANKRUPTCY COURT
NORTHERN DISTRICT OF CALIFORNIA
(SAN JOSE DIVISION)

Case No. 98-59752-MM
Chapter 7

San Jose, California
December 22, 2005, 11:00 a.m.

A.P. No. 00-5423

[Filed January 3, 2006]

In re:	)
	)
JTS CORPORATION,	)
a Delaware corporation,	)
	)
Debtor.	)
	)
SUZANNE L. DECKER,	)
	)
Plaintiff,	)
	)
v.	)
	)
JOHNSON, et al.,	)
	)
Defendants.	)
	)

TRANSCRIPT OF PROCEEDINGS

a)MOTION TO AMEND JUDGMENT BY JACK TRAMIEL, DEFENDANT

b)OPPOSITION BY SUZANNE DECKER, PLAINTIFF

BEFORE THE HONORABLE MARILYN MORGAN
UNITED STATES BANKRUPTCY JUDGE

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APPEARANCES:

NOTE: JUDGE MARILYN MORGAN APPEARS TELEPHONICALLY.

Attorneys for the Trustee:

WENDEL, ROSEN, BLACK and DEAN
BY: JEFFREY C. WURMS, ESQ.
-and-
DANIEL RAPAPORT, ESQ.
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For Jack Tramiel:

ROBINSON & WOOD
BY: CHRISTIAN B. NIELSEN, ESQ.
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San Jose, California 95113

Transcription Service:

Jo McCall
Electronic Court
Recording/Transcribing
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Gilbert, Arizona 85297
Telephone: (480-361-3790)

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P R O C E E D I N G S

December 22, 2005 11:00 a.m.

- - - oOo —

THE CLERK: This is the United States Bankruptcy Court for the Northern District of California. The court is now in session. Item 1, Decker versus Johnson.

THE COURT: Okay. Can we have the appearances of counsel, please.

MR. WURMS: Good morning, Your Honor, Jeff Wurms of Wendel Rosen for the Trustee, Ms. Decker.

MR. RAPAPORT: Good morning, Your Honor, Daniel Rapaport, accompanying Mr. Wurms.

MR. NIELSEN: Chris Nielsen for Jack Tramiel who's present in court.

THE COURT: Okay. Well, gentlemen, I really apologize to you for the fact that I'm not present. I came down with the flu and had to decide that it was the appropriate thing for me to stay home. At the same time it struck me that you all have put a great deal of work into this, and that you would want to go forward with this hearing before the end of the year.

But let me ask, is there anyone in the room who feels prejudiced by the inability to look me in the eye?

MR. WURMS: No, Your Honor.

MR. NIELSEN: No.

THE COURT: Okay. And so is there any concern about going forward with the hearing this morning?

MR. WURMS: No, Your Honor.

MR. NIELSEN: No.

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THE COURT: Okay. Then we will go forward.

Okay. Mr. Nielsen, this is your motion. Do you wish to be heard?

MR. NIELSEN: Just briefly, your Honor. In my mind, in looking at the issues, there are a number of separate causes of -- well, of separate events alleged against all of these defendants, such as a breach of

fiduciary duty, legal malpractice, fraudulent conveyance, fraud and conspiracy, that all these events combined to cause one injury, and that one injury is the economic damages allegedly flowing from the real property transaction.

Now, I think if we look at the -- three of the cases that I'd cited, the Kohn case, the Lafayette case, and the Knox case, (all phonetic), those cases all have different theories in them. In the Kohn case, it's misrepresentation of value of a home plus negligent repair of the home, and results in one injury, that injury being the purchase of the home worth less than the plaintiff believed it was worth. In that case, the court of appeal case, came back and said that the defendant was entitled to

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an offset, and even though there are these two competing theories such as misrepresentation of value and negligent repair, it only results in the one injury.

The same thing in the Lafayette case, which is an attorney malpractice case, and in a medical practice case, there are these two disparate theories that result in one injury. The overriding concern here in my mind is that where the plaintiffs claim that the defendants jointly are liable, that the offset comes to exist. The key language is "claim to have been liable." And that echoes through all of the -- through all of the cases.

So I think that there's a clear reason to provide an offset to Mr. Tramiel and I think that under Rule 59 it's certainly appropriate. There is significant damage to him, with a judgment of 1.8 million, and I think that

there's been an error in the calculation that was made in terms of whether or not this offset is appropriate.

I could go on with more of these examples of where the offset applies --

THE COURT: I basically did study all of the cases, and you're basically going over the material that's already been in your brief. So I really did study both of the briefs in this matter.

MR. NIELSEN: Okay. Then I don't have anything else to add on that, Your Honor, unless you have any

[p.6]

particular questions.

THE COURT: I don't at this time. Thank you, Mr. Nielsen.

MR. WURMS; Good morning, Your Honor, Jeff Wurms. We really don't have much to add to our papers. Our position is clear that Mr. Nielsen didn't meet the higher standard for a motion for reconsideration. We don't think that this Court overlooked anything or misunderstood anything, and he hasn't even made those allegations. And as we said in our papers, and I'll be very brief, Your Honor, the settlement credit issue really goes -- whether it's State or Federal law -- to the issue of double recovery. And when you have more than one injury in a case, if there's an allotment of settlement proceeds, the burden of proof is then on the defendant, the non-settling defendant, to show either that this results in a double recovery or that the settlement was in bad

faith, and he hasn't shown that, nor has he even shown, or has the Court found, liability.

And with regard to the option value, Your Honor, we think that Mr. Nielsen is incorrect, that the fair market value did not include a specific add-on for the one year of rents. It takes rents partially into consideration, but that's not for the one year; that's the going forward. And it also takes comparables. And that it

[p.7]

doesn't even really matter that when you do the math, as we have in our papers, the real important thing is whether there is -- with regard to the strike price and whether the Court takes into account the fact that the State loses out on the rents, which it did -- once the Court does that as my calculations show, it doesn't really matter what the fair market value is. You always come back to the same disparate consideration.

Thank you, Your Honor.

THE COURT: Okay. Thank you, Mr. Wurms. Is the matter submitted?

MR. NIELSEN: Yes, Your Honor.

MR. WURMS: Yes, Your Honor.

THE COURT: Okay. Well basically, what I heard from both of you is that you were reiterating the important points in the briefs that were filed. And by the way, your briefs were excellent and I really appreciate the time that you put into them.

MR. WURMS: Thank you, Your Honor.

THE COURT: Based on the pleadings that are before me, I am prepared at this time to go ahead and rule.

First of all, I want to thank you for raising these issues, Mr. Nielsen. Although reconsideration of a judgment is the exception and not the rule, the Federal Rule of Civil Procedures specifically allows for amendments

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to a judgment. Additionally, the Ninth Circuit has recognized that amendments are warranted to correct clear error or manifest injustice, and you all are familiar with that from the Pinion School District, Number one J, Multinoma, Camfey Oregon. (All Phonetic) So I won't give you the citation for that case.

After further reflection on the law governing settlement credits under California Code of Civil Procedures Section 877, I conclude it was error to find that defendant Tramiel was not entitled to any credit for the settlement reached by his former co-defendants. So I am going to grant the motion to amend on that basis, and I want to explain to you my reasoning.

I do not, however, believe I erred in considering the one year of rental income in determining the strike price for the option to repair the real property. Although rental income may have figured into the property's fair market value, it also was an item of

value that the Debtor would have had to relinquish in order to exercise the repurchase option.

Further, as stated in my opinion after trial, when State law forms the substance of the underlying claim, Federal Courts will apply State Court settlement procedures in determining whether a settlement credit is appropriate. I will not repeat that discussion here, but I want to note

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that in light of the State law basis for the avoidance action, I'm not persuaded by the Trustee's argument that Federal settlement procedures should apply.

Turning then to California Code of Civil Procedures Section 877, this section provides that when a settlement is reached with some, but not all, quote, "tort-feasors claim to be liable for the same tort," end quote, it shall reduce the claims against the non-settling tort-feasors, quote, "in the amount stipulated by the release, or in the amount of the consideration paid for it, whichever is greater."

The purpose of this provision is to avoid a double recovery for the same injury and here I'm citing to the same cases that Mr. Nielsen has already referenced, Maconder, Miller, Kohn, Lafayette. (All Phonetic) So as a result, whether defendants are tort-feasors claim to be liable on the same tort turns on whether their acts are claimed to have contributed to the same injury, not on whether they may be liable under the same theory of recovery.

In light of this standard, my prior determination that Section 877 was inapplicable simply because Tramiel was the only defendant named in the fraudulent conveyance claim, is wrong. As Tramiel points out, the Trustee also alleged that the settling defendants were responsible for

[p.10]

the estate's injuries arising out of the sale of the real property to Tramiel, and those claims were covered by the settlement at issue. Thus, with respect to the real property transaction, the settling defendants were tortfeasors claim to be liable for the same tort as Tramiel, the failure to pay reasonably equivalent value for the real property.

But unlike the multi-defendant single-injury cases cited by Tramiel, this case involves multiple claims for multiple injuries arising from several independent business transactions. While the Trustee claimed that the settling defendants and Tramiel were jointly liable for some of the injuries, there were other non-joint claims. Under these circumstances, settling parties can agree to allocate portions of the total settlement amount to particular claims. If done properly, the portions allocated to the non-joint claims will be excluded from the amount available for setoff by the non-settling defendant. And here I'm citing to that case that was in your briefs, Aricas versus Superior Court of San Diego County. (Phonetic). So again, I won't give you the citation on that.

To allocate a settlement on various claims, the settling parties must go beyond proving the good faith

of the settlement as a whole. They must also establish that

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the allocation itself is reasonable and in good faith. Here, I'm going to cite to a case that you all didn't. And that's L.C. Red and Son, Inc. (Phonetic) versus Superior Court, 52 Cal Ap 4th, 742, page 750, 1997.

To satisfy this burden, the parties seeking confirmation of the settlement must adequately explain the evidentiary basis for the allocation and must demonstrate that the agreed allocation was a product of adverse negotiation. Now here, I'm going to cite you to another case, Reagan Roofing Company, Inc. versus Superior Court of San Diego County, 21 Cal Ap 4th, 1685, pages 1702 through 03, a 1994 opinion in the Fourth District Court of Appeals.

The second requirement is important because without negotiated agreement, plaintiffs will naturally prefer to allocate the settlement to non-joint liabilities to maximize recovery against the non-settling defendants. The effect of a failure to show that an agreed allocation reached through adverse negotiation, frankly, is harsh. Under the plain language of California Code of Civil Procedures Section 877, settlement credits are to be, quote, "in the amount stipulated by the release or in the amount of consideration paid for it, whichever is greater." End quote.

Thus, where there is no agreed allocation, the full amount of the settlement consideration paid is

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available for setoff on all joint claims. And here I'm going to cite you to a case that I found very instructive that was not cited in your briefs. It's Alcal Roofing and Insulation versus Superior Court of San Mateo County, 8 Cal Ap 4th, 1121, pages 1126 through 27, a 1992 decision. And that case stood for the proposition that where only the plaintiff and not the settling defendants allocates the settlement, primarily to non-joint claims, the non-settling defendant is entitled to an offset for the entire amount of the other defendants' settlement.

So in this case, the Trustee contends that the settlement agreement with Mitchell Candon (Phonetic) and the attorney defendants allocated the entire settlement amount, the claims on which Tramiel is not jointly liable, the BMC stock transaction and the debt relief transaction. Now she believes none of the settlement amount is available to set off the judgment against Tramiel. I cannot agree.

While the Trustee provided adequate proof of the good faith of her overall settlement with this group of defendants, the rule was provided to establish that the allocation of the entire amount to non-joint claims was a good faith allocation reached by adverse negotiation. Significantly, the written settlement agreement merely recites that the Trustee assigned the settlement to the non-joint claims. Additionally, my order approving the

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settlement made no finding that any allocation was in good faith. In fact, the order specifically reserved the right to make allocations upon Tramiel's request for a credit, if after trial, Tramiel was liable as a joint tort-feasor on any claim for relief.

These facts are critical because they demonstrate that there was no stipulated good faith allocation. As was recognized in the Alcal Roofing case at page 1127, the Trustee's own allocation of the settlement, the claims on which Tramiel was not alleged to be jointly liable, is not enough.

So based on the principles that I've explained, I must conclude that the full amount of consideration paid in the settlement with Mitchell Candon and the attorney defendants is available to set off the judgment against Tramiel. Again, I'm going to recognize that this is a harsh result, and I struggled with why the California legislature wrote the statute to produce this outcome. As part of that struggle, I considered what I might do in terms of allocating the settlement now. If I were to undertake an allocation at this point in the case, it's likely that I would follow the judgment that I've already entered, and I realized that result would really be the same as following the plain words of the statute.

As a final matter, I'm going to note that the

[p.14]

parties dispute the value of the settlement, but there is no dispute that it is worth at least four and a half

million dollars, based on the aggregate cash amount that the settling defendants paid to the Trustee. Because that is more than enough to fully offset Tramiel's liability related to the purchase the real properties, there is no need to determine whether the settlement is worth more.

So the motion to amend the judgment is granted, and the parties should confer and submit an amended judgment in accordance with this ruling.

As a side matter, it was brought to my attention this morning that plaintiff has submitted a request to put a judgment lien -- to record a judgment lien. I wasn't aware of it until this morning coincidentally. But it strikes me that I should hold that until -- well, I don't know that at this point, you're going to be entitled to a judgment lien, Mr. Wurms.

MR. WURMS: Your Honor, I'm not aware of that request.

THE COURT: Apparently it was made in November, and if you will talk with my staff after this hearing, maybe they can show you the documents that were brought into my chambers this morning.

MR. WURMS: Okay.

THE COURT: Okay. Once again, this has been a

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long road. I have greatly appreciated the talents of the attorneys that have appeared in this matter. Thank you for your assistance.

MR. NIELSEN: Thank you, Your Honor.

MR. WURMS: Thank you, Your Honor.

THE COURT: That concludes this hearing.

(Whereupon, the proceedings are concluded at 11:18 a.m.)

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CERTIFICATE OF TRANSCRIBER

I certify that the foregoing is a correct transcript from the digital sound recording of the proceedings in the above-entitled matter.

DATED: January 3, 2006

By: /s/ Jo McCall

APPENDIX H

UNITED STATES COURT OF APPEALS
FOR THE NINTH CIRCUIT

Nos. 07-15970, 07-16004
D.C. No. CV-05-04709-JF
Northern District of California,
San Jose

[Filed October 12, 2010]

In the Matter of: JTS CORPORATION,	)
	)
Debtor,	)
	)
SUZANNE L. DECKER,	)
	)
Plaintiff - Appellee/ Cross-Appellant,	)
	)
v.	)
	)
JACK TRAMIEL,	)
	)
Defendant - Appellant/ Cross-Appellee,	)
	)
and	)
	)
ROGER W. JOHNSON; et al.,	)
	)
Defendants,	)

OFFICE OF THE U.S. TRUSTEE, Trustee,	)
v.	)
LIP-BU TAN, Third-party-defendant.	)

ORDER

Before: HUG, RYMER and McKEOWN, Circuit Judges.

The panel has voted to deny Cross-Appellant/Appellee's petition for rehearing. Judges Rymer and McKeown have voted to deny the petition for rehearing en banc, and Judge Hug has so recommended.

The full court was advised of the petition for rehearing en banc and no judge has requested a vote on whether to rehear the matter en banc. Fed. R. App. P. 35.

The petition for panel rehearing and the petition for rehearing en banc are denied.

APPENDIX I

CONSTITUTIONAL AND STATUTORY PROVISIONS INVOLVED

United States Constitution, Article I, Section 8, Clause 4

The Congress shall have power...

* * *

To establish an uniform Rule of Naturalization, and uniform Laws on the subject of Bankruptcies throughout the United States

11 U.S.C. § 544.
Trustee as lien creditor and as successor to certain creditors and purchasers

(a) The trustee shall have, as of the commencement of the case, and without regard to any knowledge of the trustee or of any creditor, the rights and powers of, or may avoid any transfer of property of the debtor or any obligation incurred by the debtor that is voidable by—

(1) a creditor that extends credit to the debtor at the time of the commencement of the case, and that obtains, at such time and with respect to such credit, a judicial lien on all property on which a creditor on a simple contract could have obtained such a judicial lien, whether or not such a creditor exists;

(2) a creditor that extends credit to the debtor at the time of the commencement of the case, and obtains, at such time and with respect to such credit, an execution against the debtor that is returned unsatisfied at such time, whether or not such a creditor exists; or

(3) a bona fide purchaser of real property, other than fixtures, from the debtor, against whom applicable law permits such transfer to be perfected, that obtains the status of a bona fide purchaser and has perfected such transfer at the time of the commencement of the case, whether or not such a purchaser exists.

(b)

(1) Except as provided in paragraph (2), the trustee may avoid any transfer of an interest of the debtor in property or any obligation incurred by the debtor that is voidable under applicable law by a creditor holding an unsecured claim that is allowable under section 502 of this title or that is not allowable only under section 502 (e) of this title.

(2) Paragraph (1) shall not apply to a transfer of a charitable contribution (as that term is defined in section 548 (d)(3)) that is not covered under section 548 (a)(1)(B), by reason of section 548 (a)(2). Any claim by any person to recover a transferred contribution described in the preceding sentence under Federal or State law in a Federal or State court shall be preempted by the commencement of the case.

11 U.S.C. § 548.
Fraudulent transfers and obligations

(a)

(1) The trustee may avoid any transfer (including any transfer to or for the benefit of an insider under an employment contract) of an interest of the debtor in property, or any obligation (including any obligation to or for the benefit of an insider under an employment contract) incurred by the debtor, that was made or incurred on or within 2 years before the date of the filing of the petition, if the debtor voluntarily or involuntarily—

(A) made such transfer or incurred such obligation with actual intent to hinder, delay, or defraud any entity to which the debtor was or became, on or after the date that such transfer was made or such obligation was incurred, indebted; or

(B)

(i) received less than a reasonably equivalent value in exchange for such transfer or obligation; and

(ii)

(I) was insolvent on the date that such transfer was made or such obligation was incurred, or became insolvent as a result of such transfer or obligation;

(II) was engaged in business or a transaction, or was about to engage in business or a transaction, for which any property remaining with the debtor was an unreasonably small capital;

(III) intended to incur, or believed that the debtor would incur, debts that would be beyond the debtor's ability to pay as such debts matured; or

(IV) made such transfer to or for the benefit of an insider, or incurred such obligation to or for the benefit of an insider, under an employment contract and not in the ordinary course of business.

(2) A transfer of a charitable contribution to a qualified religious or charitable entity or organization shall not be considered to be a transfer covered under paragraph (1)(B) in any case in which—

(A) the amount of that contribution does not exceed 15 percent of the gross annual income of the debtor for the year in which the transfer of the contribution is made; or

(B) the contribution made by a debtor exceeded the percentage amount of gross annual income specified in subparagraph (A), if the transfer was consistent with the practices of the debtor in making charitable contributions.

(b) The trustee of a partnership debtor may avoid any transfer of an interest of the debtor in property, or any obligation incurred by the debtor, that was made or incurred on or within 2 years before the date of the filing of the petition, to a general partner in the debtor, if the debtor was insolvent on the date such transfer was made or such obligation was incurred, or became insolvent as a result of such transfer or obligation.

(c) Except to the extent that a transfer or obligation voidable under this section is voidable under section 544, 545, or 547 of this title, a transferee or obligee of such a transfer or obligation that takes for value and in good faith has a lien on or may retain any interest transferred or may enforce any obligation incurred, as the case may be, to the extent that such transferee or obligee gave value to the debtor in exchange for such transfer or obligation.

(d)

(1) For the purposes of this section, a transfer is made when such transfer is so perfected that a bona fide purchaser from the debtor against whom applicable law permits such transfer to be perfected cannot acquire an interest in the property transferred that is superior to the interest in such property of the transferee, but if such transfer is not so perfected before the commencement of the case, such transfer is made immediately before the date of the filing of the petition.

(2) In this section--

(A) "value" means property, or satisfaction or securing of a present or antecedent debt of the

debtor, but does not include an unperformed promise to furnish support to the debtor or to a relative of the debtor;

(B) a commodity broker, forward contract merchant, stockbroker, financial institution, financial participant, or securities clearing agency that receives a margin payment, as defined in section 101, 741, or 761 of this title, or settlement payment, as defined in section 101 or 741 of this title, takes for value to the extent of such payment;

(C) a repo participant or financial participant that receives a margin payment, as defined in section 741 or 761 of this title, or settlement payment, as defined in section 741 of this title, in connection with a repurchase agreement, takes for value to the extent of such payment;

(D) a swap participant or financial participant that receives a transfer in connection with a swap agreement takes for value to the extent of such transfer; and

(E) a master netting agreement participant that receives a transfer in connection with a master netting agreement or any individual contract covered thereby takes for value to the extent of such transfer, except that, with respect to a transfer under any individual contract covered thereby, to the extent that such master netting agreement participant otherwise did not take (or is otherwise not deemed to have taken) such transfer for value.

(3) In this section, the term "charitable contribution" means a charitable contribution, as that term is defined in section 170(c) of the Internal Revenue Code of 1986, if that contribution—

(A) is made by a natural person; and

(B) consists of—

(i) a financial instrument (as that term is defined in section 731(c)(2)(C) of the Internal Revenue Code of 1986); or

(ii) cash.

(4) In this section, the term "qualified religious or charitable entity or organization" means—

(A) an entity described in section 170(c)(1) of the Internal Revenue Code of 1986; or

(B) an entity or organization described in section 170(c)(2) of the Internal Revenue Code of 1986.

(e)

(1) In addition to any transfer that the trustee may otherwise avoid, the trustee may avoid any transfer of an interest of the debtor in property that was made on or within 10 years before the date of the filing of the petition, if—

(A) such transfer was made to a self-settled trust or similar device;

(B) such transfer was by the debtor;

(C) the debtor is a beneficiary of such trust or similar device; and

(D) the debtor made such transfer with actual intent to hinder, delay, or defraud any entity to which the debtor was or became, on or after the date that such transfer was made, indebted.

(2) For the purposes of this subsection, a transfer includes a transfer made in anticipation of any money judgment, settlement, civil penalty, equitable order, or criminal fine incurred by, or which the debtor believed would be incurred by—

(A) any violation of the securities laws (as defined in section 3(a)(47) of the Securities Exchange Act of 1934 (15 U.S.C. 78c (a)(47))), any State securities laws, or any regulation or order issued under Federal securities laws or State securities laws; or

(B) fraud, deceit, or manipulation in a fiduciary capacity or in connection with the purchase or sale of any security registered under section 12 or 15(d) of the Securities Exchange Act of 1934 (15 U.S.C. 78l and 78o (d)) or under section 6 of the Securities Act of 1933 (15 U.S.C. 77f).

11 U.S.C. § 550.
Liability of transferee of avoided transfer

(a) Except as otherwise provided in this section, to the extent that a transfer is avoided under section 544, 545, 547, 548, 549, 553 (b), or 724 (a) of this title, the

trustee may recover, for the benefit of the estate, the property transferred, or, if the court so orders, the value of such property, from—

(1) the initial transferee of such transfer or the entity for whose benefit such transfer was made; or

(2) any immediate or mediate transferee of such initial transferee.

(b) The trustee may not recover under section (a)(2) of this section from—

(1) a transferee that takes for value, including satisfaction or securing of a present or antecedent debt, in good faith, and without knowledge of the voidability of the transfer avoided; or

(2) any immediate or mediate good faith transferee of such transferee.

(c) If a transfer made between 90 days and one year before the filing of the petition—

(1) is avoided under section 547 (b) of this title; and

(2) was made for the benefit of a creditor that at the time of such transfer was an insider; the trustee may not recover under subsection (a) from a transferee that is not an insider.

(d) The trustee is entitled to only a single satisfaction under subsection (a) of this section.

(e)

(1) A good faith transferee from whom the trustee may recover under subsection (a) of this section has a lien on the property recovered to secure the lesser of—

(A) the cost, to such transferee, of any improvement made after the transfer, less the amount of any profit realized by or accruing to such transferee from such property; and

(B) any increase in the value of such property as a result of such improvement, of the property transferred.

(2) In this subsection, "improvement" includes—

(A) physical additions or changes to the property transferred;

(B) repairs to such property;

(C) payment of any tax on such property;

(D) payment of any debt secured by a lien on such property that is superior or equal to the rights of the trustee; and

(E) preservation of such property.

(f) An action or proceeding under this section may not be commenced after the earlier of—

(1) one year after the avoidance of the transfer on account of which recovery under this section is sought; or

(2) the time the case is closed or dismissed.

Cal. Civil Code §3439.07.

(a)In an action for relief against a transfer or obligation under this chapter, a creditor, subject to the limitations in Section 3439.08, may obtain:

(1)Avoidance of the transfer or obligation to the extent necessary to satisfy the creditor's claim.

(2)An attachment or other provisional remedy against the asset transferred or its proceeds in accordance with the procedures described in Title 6.5 (commencing with Section 481.010) of Part 2 of the Code of Civil Procedure.

(3)Subject to applicable principles of equity and in accordance with applicable rules of civil procedure, the following:

(A)An injunction against further disposition by the debtor or a transferee, or both, of the asset transferred or its proceeds.

(B)Appointment of a receiver to take charge of the asset transferred or its proceeds.

(C)Any other relief the circumstances may require.

(b)If a creditor has commenced an action on a claim against the debtor, the creditor may attach the asset transferred or its proceeds if the remedy of attachment is available in the action under applicable law and the property is subject to attachment in the hands of the transferee under applicable law.

(c)If a creditor has obtained a judgment on a claim against the debtor, the creditor may levy execution on the asset transferred or its proceeds.

(d)A creditor who is an assignee of a general assignment for the benefit of creditors, as defined in Section 493.010 of the Code of Civil Procedure, may exercise any and all of the rights and remedies specified in this section if they are available to any one or more creditors of the assignor who are beneficiaries of the assignment, and, in that event (1) only to the extent the rights or remedies are so available and (2) only for the benefit of those creditors whose rights are asserted by the assignee.

Cal. Civil Code §3439.08.

(a)A transfer or an obligation is not voidable under paragraph (1) of subdivision (a) of Section 3439.04, against a person who took in good faith and for a reasonably equivalent value or against any subsequent transferee or obligee.

(b)Except as otherwise provided in this section, to the extent a transfer is voidable in an action by a creditor under paragraph (1) of subdivision (a) of Section 3439.07, the creditor may recover judgment for the value of the asset transferred, as adjusted under subdivision (c), or the amount necessary to satisfy the

creditor's claim, whichever is less. The judgment may be entered against the following:

(1)The first transferee of the asset or the person for whose benefit the transfer was made.

(2)Any subsequent transferee other than a good faith transferee who took for value or from any subsequent transferee.

(c)If the judgment under subdivision (b) is based upon the value of the asset transferred, the judgment shall be for an amount equal to the value of the asset at the time of the transfer, subject to adjustment as the equities may require.

(d)Notwithstanding voidability of a transfer or an obligation under this chapter, a good faith transferee or obligee is entitled, to the extent of the value given the debtor for the transfer or obligation, to the following:

(1)A lien on or a right to retain any interest in the asset transferred.

(2)Enforcement of any obligation incurred.

(3)A reduction in the amount of the liability on the judgment.

(e)A transfer is not voidable under paragraph (2) of subdivision (a) of Section 3439.04 or Section 3439.05 if the transfer results from the following:

(1)Termination of a lease upon default by the debtor when the termination is pursuant to the lease and applicable law.

(2)Enforcement of a lien in a noncollusive manner and in compliance with applicable law, including Division 9 (commencing with Section 9101) of the Commercial Code, other than a retention of collateral under Sections 9620 and 9621 of the Commercial Code and other than a voluntary transfer of the collateral by the debtor to the lienor in satisfaction of all or part of the secured obligation.

Ind. Code 32-18-2-18
Transferee's defenses, liability, and protections

Sec. 18. (a) A transfer or an obligation is not voidable under section 14(1) of this chapter against a person who took in good faith and for a reasonably equivalent value or against any subsequent transferee or obligee.

(b) Except as otherwise provided in this chapter, to the extent a transfer is voidable in an action by a creditor under section 17(a)(1) of this chapter, the creditor may recover judgment for the value of the asset transferred, as adjusted under subsection (c), or the amount necessary to satisfy the creditor's claim, whichever is less. The judgment may be entered against:

(1) the first transferee of the asset or the person for whose benefit the transfer was made; or

(2) any subsequent transferee other than a good faith transferee who took for value or from any subsequent transferee.

(c) If the judgment under subsection (b) is based upon the value
of the asset transferred, the judgment must be for an amount equal to the value of the asset at the time of the transfer, subject to adjustment as the equities may require.

(d) Notwithstanding voidability of a transfer or an obligation under this chapter, a good faith transferee or obligee is entitled, to the extent of the value given the debtor for the transfer or obligation, to:

(1) a lien on or a right to retain any interest in the asset transferred;

(2) enforcement of any obligation incurred; or

(3) a reduction in the amount of the liability on the judgment.

(e) A transfer is not voidable under section 14(2) or section 15 of this chapter if the transfer results from:

(1) termination of a lease upon default by the debtor when the termination is permitted by the lease and applicable law; or
(2) enforcement of a security interest in compliance with Article 9 of the Uniform Commercial Code.

As added by P.L.2-2002, SEC.3.

N.H. Rev. Stat. Ann. § 545-A:8
Defenses, Liability, and Protection of Transferee.

I. A transfer or obligation is not voidable under RSA 545-A:4, I(a) against a person who took in good faith and for a reasonably equivalent value or against any subsequent transferee or obligee.

II. Except as otherwise provided in this section, to the extent a transfer is voidable in an action by a creditor under RSA 545-A:7, I(a), the creditor may recover judgment for the value of the asset transferred, as adjusted under paragraph III, or the amount necessary to satisfy the creditor's claim, whichever is less. The judgment may be entered against:

(a) The first transferee of the asset or the person for whose benefit the transfer was made; or

(b) Any subsequent transferee other than a good faith transferee who took for value or from any subsequent transferee.

III. If the judgment under paragraph II is based upon the value of the asset transferred, the judgment must be for an amount equal to the value of the asset at the time of the transfer, subject to adjustment as the equities may require.

IV. Notwithstanding voidability of a transfer or an obligation under this chapter, a good-faith transferee or obligee is entitled, to the extent of the value given the debtor for the transfer or obligation, to

(a) A lien on or a right to retain any interest in the asset transferred;

(b) Enforcement of any obligation incurred; or

(c) A reduction in the amount of the liability on the judgment.

V. A transfer is not voidable under RSA 545-A:4, I(b) or RSA 545-A:5 if the transfer results from:

(a) Termination of a lease upon default by the debtor when the termination is pursuant to the lease and applicable law; or

(b) Enforcement of a security interest in compliance with Article 9 of the Uniform Commercial Code.

VI. A transfer is not voidable under RSA 545-A:5, II:

(a) To the extent the insider gave new value to or for the benefit of the debtor after the transfer was made unless the new value was secured by a valid lien;

(b) If made in the ordinary course of business or financial affairs of the debtor and the insider; or

(c) If made pursuant to a good-faith effort to rehabilitate the debtor and the transfer secured present value given for that purpose as well as an antecedent debt of the debtor.

UNIFORM FRAUDULENT TRANSFER ACT

§ 7. REMEDIES OF CREDITORS.

(a) In an action for relief against a transfer or obligation under this [Act], a creditor, subject to the limitations in Section 8, may obtain:

(1) avoidance of the transfer or obligation to the extent necessary to satisfy the creditor's claim;

[(2) an attachment or other provisional remedy against the asset transferred or other property of the transferee in accordance with the procedure prescribed by [ ];]

(3) subject to applicable principles of equity and in accordance with applicable rules of civil procedure,

(i) an injunction against further disposition by the debtor or a transferee, or both, of the asset transferred or of other property;

(ii) appointment of a receiver to take charge of the asset transferred or of other property of the transferee; or

(iii) any other relief the circumstances may require.

(b) If a creditor has obtained a judgment on a claim against the debtor, the creditor, if the court so orders, may levy execution on the asset transferred or its proceeds.

§ 8. DEFENSES, LIABILITY, AND PROTECTION OF TRANSFEREE.

(a) A transfer or obligation is not voidable under Section 4(a)(1) against a person who took in good faith and for a reasonably equivalent value or against any subsequent transferee or obligee.

(b) Except as otherwise provided in this section, to the extent a transfer is voidable in an action by a creditor under Section 7(a)(1), the creditor may recover judgment for the value of the asset transferred, as adjusted under subsection (c), or the amount necessary to satisfy the creditor's claim, whichever is less. The judgment may be entered against:

(1) the first transferee of the asset or the person for whose benefit the transfer was made; or

(2) any subsequent transferee other than a good-faith transferee or obligee who took for value or from any subsequent transferee or obligee.

(c) If the judgment under subsection (b) is based upon the value of the asset transferred, the judgment must be for an amount equal to the value of the asset at the time of the transfer, subject to adjustment as the equities may require.

(d) Notwithstanding voidability of a transfer or an obligation under this [Act], a good-faith transferee or obligee is entitled, to the extent of the value given the debtor for the transfer or obligation, to

(1) a lien on or a right to retain any interest in the asset transferred;

(2) enforcement of any obligation incurred; or

(3) a reduction in the amount of the liability on the judgment.

(e) A transfer is not voidable under Section 4(a)(2) or Section 5 if the transfer results from:

(1) termination of a lease upon default by the debtor when the termination is pursuant to the lease and applicable law; or

(2) enforcement of a security interest in compliance with Article 9 of the Uniform Commercial Code.

(f) A transfer is not voidable under Section 5(b):

(1) to the extent the insider gave new value to or for the benefit of the debtor after the transfer was made unless the new value was secured by a valid lien;

(2) if made in the ordinary course of business or financial affairs of the debtor and the insider; or

(3) if made pursuant to a good-faith effort to rehabilitate the debtor and the transfer secured present value given for that purpose as well as an antecedent debt of the debtor.

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In The
Supreme Court of the United States

MOHAMED POONJA, TRUSTEE, PETITIONER

v.

JACK TRAMIEL

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

BRIEF IN OPPOSITION

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QUESTIONS PRESENTED

The questions presented as stated in the petition are based on mischaracterizations of the governing law and the decision below. The questions actually presented are as stated here.

1. Section 550(a) of the Bankruptcy Code provides that in the case of a constructive fraudulent transfer, the trustee may recover either the property transferred or its value, but only "to the extent that a transfer is avoided" under the applicable provision. Section 544(b) permits the trustee to invoke state fraudulent transfer provisions, but it permits avoidance only to the extent that the transfer is "voidable under applicable [state] law." The question presented is:

> When the trustee proceeded under state law to avoid a constructive fraudulent transfer, whether the court of appeals correctly applied a state statute that expressly provides that the amount avoidable is reduced by the value of the consideration paid by the good faith transferee.

2. Section 3439.04 of the California Civil Code provides that a transfer is constructively fraudulent if, inter alia, the debtor did not receive a "reasonably equivalent value" in exchange for the transfer. Although Section 550(a) of the Bankruptcy Code permits recovery of fraudulently transferred property or its "value," recovery is expressly limited to only "the extent that a transfer is avoided" under Section 544(b) and therefore state law. Thus, here, the court

QUESTIONS PRESENTED – Continued

of appeals determined the transferred properties' "reasonably equivalent value" under the California statute. The question presented is:

> When the trustee proceeded under California law to avoid a constructive fraudulent transfer, whether the court of appeals correctly determined "reasonably equivalent value" under Section 3439.04 of the California Civil Code by reference to state law, rather than by reference to interpretations of "value" in Section 550 of the Bankruptcy Code and other provisions of federal law.

3. Section 550(d) of the Bankruptcy Code provides that a "trustee is entitled to only a single satisfaction" under Section 550(a). Section 550(a), in turn, provides that a trustee can recover only "to the extent that a transfer is avoided under section 544," which permits avoidance only to the extent that the transfer is "voidable under applicable [state] law." 11 U.S.C. § 544(b). Section 877 of the California Code of Civil Procedure provides a method for determining whether a non-settling defendant's liability should be offset by a settlement reached with other defendants. The question presented is:

> When the trustee proceeded under state law to avoid a constructive fraudulent transfer, and the trustee and other defendants settled relevant claims in connection with the transfer, whether the court of appeals correctly applied California law to determine a non-settling defendant's liability.

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INTRODUCTION

The petition for a writ of certiorari attempts to manufacture circuit conflicts, claiming one for every major issue on which petitioner lost below. But no court has recognized any of these alleged conflicts. And none of them exists. Indeed, the questions as framed in the petition are based on mischaracterizations of the governing law and the decision below. *Compare* Pet. i-ii *with* pages i-ii, *supra*.

Moreover, the court of appeals' decision is correct. The court applied the plain text of the relevant Bankruptcy Code provision, Section 544(b), which permits a trustee to avoid a transaction only to the extent that it is avoidable under state law. Under applicable state law, the court correctly concluded that respondent was not liable to petitioner.

Contrary to petitioner's claims (*e.g.*, Pet. i), the disputes at issue do not arise under Section 550 of the Bankruptcy Code. Nor did the court of appeals use its "equitable powers," as petitioner claims. Pet. i. Rather, the court merely followed applicable state law, which expressly disallows the unprecedented result sought by petitioner. In attempting to obtain review in this Court, the petition ignores the key portion of the applicable state statute. Indeed, notwithstanding petitioner's mischaracterization, the key dispute here does not even present a substantial question of federal law.

The petition for a writ of certiorari should be denied.

STATEMENT

A. Statutory Framework

1. The Bankruptcy Code gives a trustee the choice of proceeding under either federal or state law to avoid a constructive fraudulent transfer—*i.e.*, a transfer of property where the insolvent debtor did not receive reasonably equivalent value in exchange. Section 548 of the Bankruptcy Code is the federal fraudulent transfer provision and permits a trustee to avoid such fraudulent transfers under certain circumstances. Section 548(c) gives good faith transferees of constructive fraudulent transfers a lien on the transferred property "to the extent that such transferee * * * gave value to the debtor." 11 U.S.C. § 548(c). Alternatively, Section 544 permits a trustee to invoke state fraudulent transfer provisions. Section 544(b) provides that "the trustee may avoid any transfer of an interest of the debtor in property or any obligation incurred by the debtor that is voidable under applicable law." *Id.* § 544(b)(1). Here, relying on Section 544(b), petitioner pursued claims against respondent under California Civil Code § 3439 et seq., California's version of the Uniform Fraudulent Transfer Act.

If a transfer is avoidable under Section 544 or Section 548, then Section 550 gives the trustee the option to recover either the property itself or its value: "Except as otherwise provided in this section, * * * the trustee may recover, for the benefit of the estate, the property transferred, or, if the court so orders, the value of such property * * * ." *Id.* § 550(a).

But under Section 550, the trustee may recover only "to the extent that a transfer is avoided under [state law through] section 544 * * * [or federal law through] 548." *Ibid.* Thus, when (as here) state law expressly bars liability, then no liability arises—notwithstanding Section 550's "[e]xcept as otherwise provided herein" language—because there is liability under Section 550 only "to the extent that" it arises under state law incorporated by Section 544.

2. Section 3439.04 of the California Civil Code establishes whether a particular transfer was constructively fraudulent. It provides that "[a] transfer made or obligation incurred by a debtor is fraudulent as to a creditor * * * if the debtor made the transfer or incurred the obligation" "[w]ithout receiving a reasonably equivalent value in exchange for the transfer or obligation, and the debtor" "[i]ntended to incur, or believed or reasonably should have believed that he or she would incur, debts beyond his or her ability to pay as they became due." Cal. Civ. Code § 3439.04(a)(2)(B).[1]

Section 3439.07 establishes the extent to which a fraudulent transfer is voidable under California law (and, therefore, under Section 544 of the Bankruptcy Code). It provides that "a creditor, *subject to the*

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[1] As the petition appendix does not include Section 3439.04 of the California Civil Code or Section 877 of the California Code of Civil Procedure, they are attached in an appendix to this brief in opposition.

limitations in Section 3439.08, may obtain," inter alia, "[a]voidance of the transfer or obligation to the extent necessary to satisfy the creditor's claim." *Id.* § 3439.07(a)(1) (emphasis added).

Section 3439.08, which expressly limits Section 3439.07, provides that if the fraudulent transfer was made to a good faith transferee (as here), the voidable amount is reduced by the value of the purchase price that the transferee paid: "Notwithstanding voidability of a transfer or an obligation under this chapter, a good faith transferee or obligee is entitled, to the extent of the value given the debtor for the transfer or obligation, to * * * [a] reduction in the amount of the liability on the judgment." *Id.* § 3439.08(d)(3). Were it otherwise, the trustee would obtain a double recovery by retaining the value already paid in addition to recovering the value of the transfer.

B. Factual Background

Respondent Jack Tramiel was the chairman of the board of directors of Atari Corporation ("Atari") in 1996, when Atari merged with and into JTS Corporation ("JTS"). As part of the merger, Tramiel became a director of JTS. The primary purpose of the JTS-Atari merger was to provide working capital to JTS, which was in dire financial straits. Pet. App. 4a.

In the merger, JTS was set to acquire, inter alia, eight separate pieces of Atari's real estate located in California and Texas that were not needed by JTS. To generate additional capital, JTS's chief financial

officer urged that Tramiel purchase these pieces of property. Tramiel agreed to purchase the properties for $10 million and to give JTS a one-year option to repurchase the property for $10 million. If JTS had exercised the option, then Tramiel would have kept the greater of $1 million or the rental income generated by the property during the one-year option period. *Id.* at 4a-5a.

The deal was supported by JTS's outside counsel, and JTS's board of directors approved it in June 1996. Although Tramiel was a member of the board, he recused himself from the decision and was not present for boardroom discussions about the proposed transaction. *Id.* at 5a. Tramiel told the board that they should obtain an independent assessment of the value of the properties. *Id.* at 71a. JTS's board ultimately concluded that the sale to Tramiel was the quickest and most efficient way to raise the additional capital needed to keep JTS afloat. The board recognized that selling the pieces of property individually on the open market would likely generate more capital than the package sale to Tramiel. *Id.* at 5a. But because JTS urgently needed the funding, the board believed the overall deal to be fair and in JTS's best interests. The sale closed in September 1996. *Ibid.*

JTS marketed the properties for sale during the one-year option period but never found a buyer and never exercised the option. The parties stipulated that the properties generated net rental income of $1,387,185 during the option period. *Id.* at 72a-73a.

JTS took several other steps to generate funding to stay in business. All of JTS's efforts, however, proved unsuccessful. In November 1998, JTS was forced into bankruptcy through an involuntary petition. JTS then filed a Chapter 11 petition, which was converted to one under Chapter 7 in 1999. *Id.* at 5a. Thereafter the bankruptcy trustee appointed in the case sued various parties, including Tramiel and many other participants in the sale of the properties.

C. Proceedings Below

1. Proceedings in the bankruptcy court

a. The bankruptcy trustee brought this action in 2003 against Tramiel, the other JTS directors, JTS's attorneys, and a JTS shareholder. Pet. App. 65a. As relevant here, the trustee claimed that the sale of the real estate to Tramiel was a fraudulent transfer and sought avoidance under Section 544. All defendants except Tramiel reached a settlement with the trustee and agreed to pay the estate a total of at least $4.5 million. *Id.* at 6a.

b. After trial, the bankruptcy court found in 2005 that the sale of the properties to Tramiel was avoidable as a constructive fraudulent conveyance under Section 544(b) of the Bankruptcy Code and Section 3439.04(a) of the California Civil Code. *Id.* at 84a. The court held that Tramiel did not give JTS a reasonably equivalent value for the properties.

The bankruptcy court found that the value of the properties would have been $15,760,000 if they had

been sold separately after being exposed to the market for a year. *Id.* at 85a. But because the properties were sold as a bundle, the court found, "[a]fter careful consideration of the presentations by both [sides'] experts, * * * that a 20% discount for bundling the properties is appropriate." *Id.* at 86a. The court also found that "a further 5% discount should be applied for the quick sale." *Ibid.* The court stated that the discounts "make[ ] sense because the buyer accepts the risk of less attractive properties that are bundled with the more valuable pieces and because the seller loses the competitive benefit of a normal marketing period." *Ibid.*

The court rejected the trustee's argument that no discount should apply because Tramiel insisted on purchasing the entire portfolio and because there was no financial need to complete the sale so quickly: "[T]he evidence establishes that JTS wanted both a bundled sale and a quick sale." *Ibid.* It was JTS, not Tramiel, that "set the original tone of this transaction as a bundled sale." *Ibid.* Additionally, "JTS had been insolvent for some months and its financial condition was deteriorating rapidly. The company needed cash and needed it quickly to fund continued operations." *Ibid.* The court found that "JTS was willing to accept something less than the best price to get cash fast." *Id.* at 87a. Applying both discounts, the court found the value of the portfolio to be $11,820,000. *Id.* at 88a.

To determine whether Tramiel gave JTS reasonably equivalent value, the bankruptcy court added

together the $10 million in cash that Tramiel paid, plus the value of the one-year repurchase option that Tramiel gave JTS. *Ibid.* The court calculated the value of the repurchase option by subtracting the strike price of the repurchase option (the amount JTS had to pay to exercise the option) from the properties' value. *Id.* at 88a-89a. Although JTS had to pay only $10 million to exercise the option, the court held that the actual strike price was $10 million plus the rental income during the option period because "to exercise the option, JTS not only had to pay $10 million, it also had to relinquish all rights it had to $1,387,185, the option year's net rental income from the properties." *Id.* at 89a. The court therefore found the strike price to be $11,387,185. *Ibid.* The court thus determined the price of the option to be $432,815—the properties' value of $11,820,000 minus the strike price of $11,387,185. *Ibid.*

Adding together the cash that Tramiel paid ($10 million) and the value of the option ($432,815), the bankruptcy court found that Tramiel paid JTS a total consideration of $10,432,815 for the properties. *Ibid.* Because of the difference between the $11,820,000 value of the properties and the $10,432,815 that Tramiel paid in good faith, the court held that JTS did not receive reasonably equivalent value for the properties and that the transaction was avoidable as a constructive fraudulent conveyance. *Id.* at 89a-90a.

c. The bankruptcy court then calculated Tramiel's liability and explained the rationale for its rulings.

The trustee argued that under Section 550 of the Bankruptcy Code, Tramiel should be liable for the full value of the properties transferred, $11,820,000, rather than the difference between the $11,820,000 value and the $10,432,815 that Tramiel already had paid.

The bankruptcy court rejected that argument. The court noted that Section 544 of the Bankruptcy Code "merely allows a bankruptcy trustee to assert avoidance powers that are otherwise available under state law." *Id.* at 90a. Thus, "the trustee may only avoid the real properties to the extent permitted in § 3439.07" of the California Civil Code. *Ibid.* Section 3439.07(a)(1) provides that "the ability to avoid a transfer is expressly subject to the limitations set forth in § 3439.08." *Ibid.* One such limitation in Section 3439.08 is that "a good faith transferee is entitled, to the extent of the value given the debtor for the transfer, to a reduction in the amount of liability on the judgment." *Id.* at 91a. Thus, "if Tramiel is a good faith transferee, the transaction may only be avoided to the extent that the value of the real properties exceeded the value that Tramiel gave to JTS." *Ibid.*

The court found that Tramiel was a good faith transferee. The court stated that "there is no evidence that Tramiel intended to take advantage of JTS when he purchased the portfolio of real property." *Ibid.* "Rather, the evidence is overwhelming that Tramiel honestly believed that he was helping the company by allowing it to get immediate access to

cash, while protecting it if JTS could ultimately find a buyer willing to pay a higher price." *Ibid.*

Therefore, the court calculated Tramiel's liability as the difference between the value of the properties and the value of what Tramiel paid: $1,387,185. *Ibid.*

d. The bankruptcy court held that Tramiel was entitled to a credit against that liability on account of the $4.5 million settlement that his co-defendants already had paid the estate. *Id.* at 143a. In so doing, the bankruptcy court applied California law, Section 877 of the California Code of Civil Procedure. The court stated that "when State law forms the substance of the underlying claim, Federal Courts will apply State Court settlement procedures in determining whether a settlement credit is appropriate." *Id.* at 144a; *see also id.* at 114a. Under Section 877, when a settlement is reached with some but not all "tortfeasors claimed to be liable for the same tort," it reduces the claims against the non-settling tortfeasors "in the amount stipulated by the release * * * or in the amount of the consideration paid for it whichever is the greater." Cal. Civ. Proc. Code § 877(a); *see also* Pet. App. 144a. The purpose of this provision is "to avoid a double recovery for the same injury." Pet. App. 144a.

The bankruptcy court held that the settling defendants and Tramiel were all joint tortfeasors, because the trustee "also alleged that the settling defendants were responsible for the estate's injuries arising out of the sale of the real property to Tramiel." *Id.* at 145a. Thus, at least some of the settlement

amount would be available to satisfy the claim against Tramiel.

To determine how much of the settlement to allocate to the claims arising out of the property sale to Tramiel, the bankruptcy court noted that "settling parties can agree to allocate portions of the total settlement amount to particular claims," and "the portions allocated to the non-joint claims will be excluded from the amount available for setoff by the non-settling defendant." *Id.* at 145a. But here, when the trustee entered into the settlement with the other defendants, the parties did not allocate the total settlement between particular claims. The court stated that under the "plain language" of Section 877, "where there is no agreed allocation, the full amount of the settlement consideration paid is available for setoff on all joint claims." *Id.* at 146a-147a. Thus, the court held that the full $4.5 million in consideration paid in the settlement was available to offset the judgment against Tramiel. *Id.* at 148a.

The bankruptcy judge further stated that if she were actually to allocate the settlement among the joint and non-joint claims, the result would be the same: "I considered what I might do in terms of allocating the settlement now. If I were to undertake an allocation at this point in the case, it's likely that I would follow the judgment that I've already entered, and I realized that result would really be the same as following the plain words of the statute." *Ibid.*

Because the $4.5 million settlement amount was "more than enough to fully offset Tramiel's liability related to the purchase of the real properties," the bankruptcy court held that the trustee could recover nothing from Tramiel. *Id.* at 149a.

2. Proceedings in the district court

The district court affirmed in part and reversed in part.

a. As to whether Tramiel's liability could be reduced by the value of the consideration Tramiel paid to JTS as a good faith purchaser, the district court held that "the bankruptcy court properly permitted Tramiel to set off the value he gave for the properties when adjudicating his liability." *Id.* at 52a. The district court also "ha[d] no difficulty concluding that the bankruptcy court's finding of good faith was not clearly erroneous." *Ibid.*

b. In calculating Tramiel's liability, however, the district court held that "fair market value is the appropriate starting point." *Ibid.* Thus, the court calculated the properties' value as $15,760,000, without any discount for bundling and a quick sale, plus the option-period rents of $1,387,185. The court determined the properties' "total fair market value" to be $17,147,185. *Id.* at 53a.

The district court thus calculated Tramiel's liability as the $17,147,185 value of the properties minus the $10,432,815 in consideration that Tramiel paid JTS, for a total liability of $6,714,370. *Ibid.*

c. As to the settlement credit, the district court also applied California law but held that Tramiel was not entitled to any credit for the $4.5 million settlement. The court held that the settlement agreement allocated the settlement funds to claims other than the claim against Tramiel. *Id.* at 56a.

3. Proceedings before the court of appeals

A unanimous court of appeals agreed with the bankruptcy court's decision and affirmed it in full.

a. The court of appeals held that the bankruptcy court's finding that the properties' value was $11,820,000 was not clearly erroneous. *Id.* at 11a. The court explained that under Section 544(b)(1) of the Bankruptcy Code, a transfer may be avoided only to the extent that it may be avoided under state law. And under Section 3439.04(a) of the California Civil Code, a transfer is avoidable to the extent the debtor did not receive a "reasonably equivalent value." *Id.* at 10a.

In determining reasonably equivalent value, California law permits courts to "consider the fair market value or what would be the fairly equivalent value of the property, taking into consideration all of the specific circumstances of each case affecting the value of the asset." *Id.* at 10a-11a. Thus, the bankruptcy court did not clearly err by applying a 5% reduction for a quick sale and a 20% reduction for

a bundled sale. *Id.* at 11a. The court of appeals reasoned: "Evidence showed that JTS wanted immediate cash and was willing to take a reduced price for the real property to obtain the funds quickly." *Ibid.* "JTS wanted a quick and bundled sale and even [the trustee's] expert agreed that reductions for a quick and bundled sale were proper if a seller required those terms." *Ibid.*

The court of appeals also concluded that the bankruptcy court did not clearly err in finding that the value of the repurchase option was $432,815 under those circumstances. *Id.* at 12a.

b. The court of appeals agreed with both the district court and the bankruptcy court that Tramiel's liability should be reduced by what he paid JTS as a good faith purchaser under Section 3439.08 of the California Civil Code. The court of appeals rejected the trustee's novel argument that "the interplay of §§ 544(b) and 550 requires full avoidance, and that California Civil Code § 3439.08(d)(3) is not applicable because" it "cannot limit the transferee's avoidance." *Id.* at 20a.

The court reasoned that the text of Sections 544 and 550 require California law to be applied to calculate the amount that may be avoided. *Id.* at 15a. The court explained that Section 550 authorizes recovery of the value of the property transferred, but only to the extent it is avoided under Section 544. *Ibid.* And Section 544 allows the trustee to avoid only a transfer that could have been avoided under applicable state

law. *Id.* at 14a. Section 3439.07 of the California Civil Code "allows relief of avoidance 'to the extent necessary to satisfy the creditor's claim,'" but that "is expressly made 'subject to the limitations in Section 3439.08'—and those limitations include a reduction for what a good faith transferee paid." *Id.* at 20a (quoting Cal. Civ. Code § 3439.07). Further, this result is consistent with the intent of Section 550: "The purpose of § 550 is to restore the estate to the financial condition it would have enjoyed if the transfer had not occurred." *Id.* at 15a (citation omitted). The court of appeals noted that this result is consistent with the similar protection afforded good faith buyers under Section 548(c). *Id.* at 25a.

c. The court of appeals also held that the $4.5 million settlement offset Tramiel's $1,387,185 liability. As the bankruptcy court and the district court both did, the court of appeals applied Section 877 of the California Code of Civil Procedure.

The court of appeals agreed with the bankruptcy court that Tramiel and the settling defendants were jointly liable: "Here, the trustee alleged Tramiel and the settling defendants combined to carry out the same injury, *i.e.*, the fraudulent transfer of the real property. * * * It is irrelevant that the trustee alleged different torts against Tramiel and the settling defendants since their concerted conduct produced the same injury * * * ." *Id.* at 29a. And the court held that under Section 877, because there was "no stipulated good faith allocation" in the agreement, Tramiel

was "entitled to an offset * * * of the entire settlement amount paid to the trustee." *Id.* at 32a.

Because the $4.5 million settlement credit exceeded Tramiel's liability, the court held that "Tramiel has no liability to the trustee for the conveyance." *Id.* at 33a.

REASONS THE PETITION SHOULD BE DENIED

I. NO CIRCUIT CONFLICT EXISTS AS TO WHETHER, WHEN USING STATE LAW TO AVOID A TRANSFER UNDER SECTION 544(b), STATE LAW GOVERNS THE AMOUNT THAT MAY BE AVOIDED, AND THE DECISION BELOW IS CORRECT

Contrary to petitioner's assertion, no conflict among the circuits exists as to the question whether a good faith transferee of property found to have been constructively fraudulently conveyed may "assert defenses not otherwise provided in § 550" of the Bankruptcy Code. Pet. i (emphasis omitted). In fact, Tramiel did not assert a "defense" under Section 550 in the manner that petitioner suggests. Rather, he asserted that he was not liable in the first instance because, under Section 550(a), recovery is permitted only to the "extent that a transfer is avoided" under state law through Section 544. As all three courts below correctly held that because Tramiel was a good faith transferee, Section 3439.08 of the California Civil Code reduces the amount that may be avoided under California law by the value of what Tramiel

paid JTS. That decision, which ultimately turns on state rather than federal law, does not warrant this Court's review.

A. There Is No Conflict Among The Courts Of Appeals

1. Petitioner claims that the decision below conflicts with five decisions from courts of appeals supposedly holding that "initial transferees are strictly liable and may not assert defenses that § 550 does not expressly provide." Pet. 12. But those decisions do not address the issue here. Rather, the question at issue in those cases was whether, under Section 550, the defendant was an *initial* transferee or a *subsequent* good faith transferee.

Under Section 550(a), the trustee may recover the fraudulently transferred property or its value from "(1) the initial transferee" or "(2) any immediate or mediate transferee of such initial transferee." 11 U.S.C. § 550(a). But Section 550(b) gives a defense to liability to certain "immediate or mediate" transferees (*i.e.*, someone who received the property from the initial transferee). Section 550(b) provides that "[t]he trustee may not recover under section (a)(2) of this section from" "(1) a transferee that takes for value * * * in good faith, and without knowledge of the voidability of the transfer avoided" or "(2) any immediate or mediate good faith transferee of such transferee." *Id.* § 550(b).

The issue in the cases cited by petitioner was thus whether that Section 550(b) defense applied—*i.e.*,

whether the transferee was a *subsequent* good faith transferee with immunity or an *initial* transferee who was strictly liable. *See, e.g.*, *In re Red Dot Scenic, Inc.*, 351 F.3d 57, 58 (2d Cir. 2003) (holding defendant "was not the initial transferee"); *In re Hurtado*, 342 F.3d 528, 536 (6th Cir. 2003) (holding defendant had "the requisite dominion and control over the disputed funds as to make her an initial transferee"). That question involves whether a trustee can recover on an avoidable transaction from a particular defendant, *not* whether the transaction itself is avoidable and, if so, in what amount. *See, e.g.*, *Hurtado*, 342 F.3d at 532 (quoting *Suhar v. Burns*, 322 F.3d 421, 427 (6th Cir. 2003) ("explaining that 'avoidance and recovery are distinct concepts and processes' that 'are addressed in two separate sections of the code' ").

Here, there is no dispute that respondent Tramiel was an initial transferee and thus cannot invoke the Section 550(b) complete defense to liability. But he is strictly liable only for the amount that is avoidable under California law *after* applying the Section 3439.08 reduction for the value he paid JTS. The cases petitioner cites do not hold otherwise.

2. Nor does the decision below conflict with the Seventh Circuit's decision in *Boyer v. Crown Stock Distribution, Inc.*, 587 F.3d 787 (7th Cir. 2009). Pet. 13-14. Like the above cases, *Boyer* determined that the Section 550(b) defense was unavailable because the transferees were initial, rather than subsequent, transferees. *Boyer*, 587 F.3d at 796-797.

Boyer involved a leveraged buyout masked as a sale of a corporation's assets. A closely held corporation sold all of its assets to a newly formed corporation that was given the same name. *Id.* at 790, 793. In exchange, the new corporation paid $3.1 million that it had taken as a loan, using the "purchased" assets as collateral. *Ibid.* The original corporation distributed the money to its shareholders—all of whom were members of the same family—and then ceased operations. *Id.* at 791. The new corporation later filed for bankruptcy. When the $3.1 million payment was challenged, the bankruptcy court held that the payment to the original corporation was a fraudulent transfer. *Ibid.* On appeal, the Seventh Circuit held that the two transactions—(1) the sale of assets in exchange for $3.1 million and (2) the distribution of the $3.1 million to the shareholders—should be "collapsed" and viewed as a single transaction. *Id.* at 796. As such, the shareholders were initial transferees of the $3.1 million, not subsequent transferees, and the Section 550(b) defense was unavailable to them. *Id.* at 796-797.

Petitioner asserts that *Boyer* conflicts with the court of appeals' decision in this case because the Seventh Circuit "without discussion" rejected the shareholders' argument that their liability should be reduced by the value of the assets sold to the new corporation. Pet. 14-15. Petitioner's claim of a conflict relies on the Seventh Circuit's statement: "The defendants make some other arguments, but they do not require discussion." *Boyer*, 587 F.3d at 798. Such

a statement does not create a conflict warranting this Court's review.

Moreover, and in any event, there is no tension between *Boyer* and the court of appeals' decision here. In another part of the opinion, *Boyer* states that the shareholders "gave *nothing* in exchange for their [$3.1 million in] distributions." *Id.* at 796 (emphasis added). Indeed, the leveraged buyout was a fraudulent transfer because "in exchange for the money the shareholders received, they provided *no value* to the corporation but merely increased its debt and by doing so pushed it over the brink." *Id.* at 792 (emphasis added). Because the shareholders paid nothing, their liability could not have been reduced by their payment amount. By contrast, here it is beyond dispute that, in exchange for the properties, Tramiel gave JTS $10 million plus the value of the option.

3. Finally, there is no disagreement between the ruling below and the Ninth Circuit's prior opinion in *In re Straightline*, 525 F.3d 870 (9th Cir. 2008). Even if there were, such an intracircuit conflict would not merit this Court's review. In *Straightline*, there was no avoidance under state law pursuant to Section 544(b). Rather, the transfer found to have been fraudulent was a *post*petition transfer that was avoided under Section 549 of the Bankruptcy Code. *Straightline*, 525 F.3d at 877.

Section 549 provides that the trustee may avoid a postpetition transfer of property of the estate "that is not authorized under this title or by the court." 11

U.S.C. § 549(a)(2)(B). Unlike California law, Section 549 contains no provision limiting the amount that may be avoided by the value that the transferee gave the debtor, and it is on that basis that the court denied such a reduction. *See Straightline*, 525 F.3d at 884 (citing another Section 549 decision, *Walsh v. Alpha Fin. Group* (*In re Rice*), 83 B.R. 8, 13 (B.A.P. 9th Cir. 1987)).

Moreover, unlike here, the transferee would not have been entitled to any "good faith" exception because the bankruptcy court found that the transaction "was a disguised loan in contravention of [the court's] earlier order." *Id.* at 885. The court thus did not hold that such a reduction would never be applicable, but rather that it was not available in that case because "the estate ha[d] a greater equitable claim than" the defendant. *Id.* at 884.

B. The Decision Below Correctly Held That Section 3439.08 Of The California Civil Code Reduces The Amount That The Trustee May Avoid

1. The decision of the court of appeals is correct. And, contrary to petitioner's argument, it is fully supported by the text of Sections 544 and 550 of the Bankruptcy Code. As the court of appeals explained (Pet. App. 14a-15a), Section 550(a) provides that the trustee may recover from initial transferees either the property transferred or the value of such property, but only "to the extent that a transfer is avoided under section 544." 11 U.S.C. § 550(a). And under

Section 544(b), the provision invoked in this case, the trustee may avoid "an interest of the debtor in property" but only to the extent it "is voidable under applicable law"—*i.e.*, state law. *Id.* § 544(b).

Under the state law applicable here, the voidable amount is limited to the difference between the value of the property transferred and the consideration given. Section 3439.07(a) of the California Civil Code permits avoidance of a fraudulent transfer, but such avoidance is expressly made "subject to the limitations in Section 3439.08." Cal. Civ. Code. § 3439.07(a). Section 3439.08 provides that "a good faith transferee * * * is entitled, to the extent of the value given for the debtor for the transfer * * * , [a] reduction in the amount of the liability on the judgment." *Id.* § 3439.08(d)(3).

Thus, all three courts below correctly concluded that because Tramiel was a good faith transferee, the trustee could avoid only the difference between the properties' value and what Tramiel paid for them.

2. Contrary to petitioner's assertion, the court of appeals did not "invoke [its] equitable powers," (Pet. i), or grant Tramiel an "equitable remed[y]," (Pet. 20). Rather, after applying state statutory law as required by the text of the Bankruptcy Code, the court simply observed that its conclusion was consistent with the Code's purposes: "This conclusion effectuates the intent of § 550 to restore the bankrupt estate to the financial condition it enjoyed prior to the transfer." Pet. App. 25a. And the court stated that "[a]llowing

the estate to profit by taking value that should be returned to a good faith transferee does not promote the purpose of § 550 to restore equity." *Ibid.* But the court's holding did not rely on equitable principles; rather, it relied on the text of Sections 544 and 550 and the California fraudulent transfer statutes.

Nor did the decision below "rel[y] on a novel belief that § 550 silently incorporates the [good faith] defense provided in § 548(c) because § 544(b) and § 548 transferees must be subject to symmetrical recoveries." Pet. 21. Rather, the court of appeals merely observed at the end of its discussion that its decision "permits a symmetry with the Bankruptcy Code." Pet. App. 25a. The court of appeals did not hold that the recoveries available under state law through Section 544(b) must be the same as those available under federal law in Section 548.

3. Section 548 highlights, however, that petitioner's unprecedented legal theory would contravene the policies of both federal bankruptcy law and state law, by allowing a double recovery for the estate. Both state and federal law fully protect buyers from losses arising from purchases made in good faith if the purchases are later avoided. *See* Cal. Civ. Code. § 3439.08 (providing good faith purchasers a credit for their purchase price); 11 U.S.C. § 548(c) (giving good faith purchasers a lien on the purchased asset to the extent of the purchase price). Yet petitioner seeks to force Tramiel to pay the full $11.8 million value of the purchased property—actually, more, because petitioner contends the value exceeds that amount—even

though the estate retains the original $10.4 million Tramiel already paid. No authority supports petitioner's notion that Sections 544 and 550 should be read to require a double recovery to the estate when a trustee proceeds under state law.

Moreover, a rule requiring good faith purchasers to pay twice for an avoided transfer would create a strong disincentive to transact with businesses in financial distress. Distressed companies often rely on the ability to convert surplus assets into operating capital by selling them to willing purchasers. But under petitioner's rule, this safeguard would be severely limited, as good faith purchasers would be unable to rely on the protections provided by existing law. Indeed, despite their good faith, purchasers would risk being saddled with a double payment for the purchased asset, even if a bankruptcy judge later determined that the original purchase price was only marginally less than the asset's reasonably equivalent value. Although the purchaser would have an unsecured claim under Section 502(h) of the Bankruptcy Code for the value of the payment made, *see* 11 U.S.C. § 502(h), that negligible prospect for recovery would be insufficient to encourage good faith purchasers to aid struggling companies. Unsecured creditors in Chapter 7 often receive only pennies on the dollar for their claims. Petitioner's proposed new rule thus would hamper distressed companies' ability to raise working capital in troubled economic times.

II. THE COURT OF APPEALS CORRECTLY APPLIED CALIFORNIA'S DEFINITION OF "REASONABLY EQUIVALENT VALUE," AND THAT DECISION DOES NOT CONFLICT WITH ANY DECISION OF THIS COURT OR ANY COURT OF APPEALS

A. There Is No Conflict Among The Courts Of Appeals

1. Petitioner argues that the decision below creates a conflict among the circuits over the definition of "value" in Section 550 of the Bankruptcy Code. Pet. 22. But in affirming the bankruptcy court's calculation of the properties' reasonably equivalent value, the court of appeals was not interpreting "value" in Section 550; rather, it was interpreting and applying "reasonably equivalent value" in Section 3439.04 of the California Civil Code. Its decision therefore does not present a question of federal law and could not have created the conflict that petitioner claims.

Because petitioner invoked Section 544(b) of the Bankruptcy Code to seek avoidance, the court of appeals was required to look to applicable California law. As the opinion below explains, "[u]nder California Civil Code § 3439.04(a), a transfer is avoidable if," inter alia, "the debtor made the transfer without receiving a *reasonably equivalent value*." Pet. App. 10a (emphasis added). And the court explained that under California law, reasonably equivalent value may be "the fair market value *or* what would be the fairly equivalent value of the property, taking into

consideration all of the specific circumstances of each case affecting the value of the asset." *Id.* at 10a-11a (emphasis added) (citing *Hansen v. Cramer*, 245 P.2d 1059 (Cal. 1952); *Bailey v. Leeper*, 298 P.2d 684 (Cal. Ct. App. 1956)). Thus, in determining the extent to which the transfer was avoidable, the court considered the properties' reasonably equivalent value in light of the fact that the properties were bundled together and sold quickly. *Id.* at 11a-12a.

2. Petitioner claims that the court of appeals' calculation of the "reasonably equivalent value" of the JTS properties conflicts with this Court's decisions in *BFP v. Resolution Trust Corp.*, 511 U.S. 531 (1994), and *Associates Commercial Corp. v. Rash*, 520 U.S. 953 (1997). Petitioner asserts that those decisions hold that "value" in Section 550 "means either a property's fair market value or, in very limited cases, its foreclosure sale price." Pet. 22-23 (emphasis omitted). Thus, petitioner argues that the court below should have used "fair market value" rather than "reasonably equivalent value."

But *BFP* and *Rash* are inapposite because they interpreted provisions of federal law, not the state law provision at issue here. *BFP* interpreted the meaning of "reasonably equivalent value" in Section 548 of the Bankruptcy Code, which permits the trustee to avoid a fraudulent transfer made within two years before the date of the filing of the petition (but protects a good faith buyer by providing a lien under Section 548(c)). 511 U.S. at 535. And *Rash* construed "value" in Section 1325(a)(5)(B) of the

Bankruptcy Code—the Code's "cram down" provision. 520 U.S. at 955-956. This Court's interpretations of those provisions do not govern the interpretation of "reasonably equivalent value" in Section 3439.04(a) of the California Civil Code, as incorporated into Section 544 of the Bankruptcy Code.

Regardless, the court of appeals' decision is in harmony with *BFP* and *Rash*. This Court held in *BFP* that the reasonably equivalent value of property sold at foreclosure is not necessarily the full "fair market value" or the price that could be obtained "if it did not have to be sold within the time and manner strictures of state-prescribed foreclosure." 511 U.S. at 539. The Court reasoned that "property that must be sold within those strictures is simply worth less." *Ibid.* (emphasis omitted). That is because "[n]o one would pay as much to own such property as he would pay to own real estate that could be sold at leisure and pursuant to normal marketing techniques." *Ibid.* Thus, courts need not "ignore that characteristic of the property," just as they would not "ignore other price-affecting characteristics." *Ibid.*

Likewise, in *Rash*, after the Court decided that "value" of a car in Section 1325(a)(5)(B) means the car's "replacement value," the Court stated that it would "leave[ ] to bankruptcy courts, as triers of fact, identification of the best way of ascertaining replacement value on the basis of the evidence presented." 520 U.S. at 965 n.6. The Court explained that bankruptcy courts might need to make "adjustment[s]" to the

car's retail price in view of the individual circumstances of each case. *Ibid.*

Just as *BFP* and *Rash* held that bankruptcy courts, as factfinders, need not ignore circumstances that affect the value of property, the bankruptcy court below was free to find that the properties JTS sold to Tramiel were worth less because they were sold quickly and as a bundle.

In any event, at bottom, petitioner's complaint is actually about the court of appeals' interpretation of California's "reasonably equivalent value" standard. This Court's review of that state law question is not warranted. *See* S. Ct. R. 10; *see also Cort v. Ash*, 422 U.S. 66, 72 n.6 (1975) (this Court's "practice of deference" to the courts of appeals' "determinations of questions of state law * * * should generally render unnecessary review of their decisions in this respect").

3. Nor does the decision below conflict with any of the other decisions cited by petitioner. Pet. 24-25.

In re Taylor, 599 F.3d 880 (9th Cir. 2010), is an opinion from the Ninth Circuit; thus, any conflict would, at most, be an intracircuit conflict not warranting this Court's review. Moreover, the court in *In re Taylor* stated that the "bankruptcy court * * * has *discretion* on how to value the property so as to put the estate in its pretransfer position." 599 F.3d at 890 (emphasis added). Such discretion is incompatible with petitioner's inflexible fair-market-value-only approach.

And the passing reference to "market value" in *In re Trout*, 609 F.3d 1106, 1112 (10th Cir. 2010), does not conflict with the decision below. Petitioner acknowledges that the reference is "dicta." Pet. 25. The issue in *Trout* was whether, after finding a fraudulent transfer, the bankruptcy court must order recovery of some property or its value under Section 550 or may conclude that the automatic lien avoidance provision in Section 551 adequately protects the estate. 609 F.3d at 1107-1108. *Trout* did not discuss whether "fair market value" or "reasonably equivalent value" was the correct measure. *See id.* at 1112.

Petitioner's citations to opinions from bankruptcy courts (Pet. 25) do not merit extended discussion, as any disagreement among the bankruptcy courts does not warrant this Court's review. In any event, as in *Trout*, neither of those decisions involved whether "fair market value" or "reasonably equivalent value" was the correct measure after avoidance under Section 544(b).

B. Even If There Were A Disagreement Among The Circuits, This Case Would Not Be A Suitable Vehicle To Resolve It

Even if the court of appeals had agreed with petitioner and used the properties' undiscounted value ($17,147,185) rather than the reasonably equivalent value after the bundling and quick-sale discounts ($11,820,000), the outcome of this case would have been unchanged.

Tramiel's liability, before applying the settlement credit, is the difference between the properties' value and the value of what Tramiel paid. Pet. App. 24a. Tramiel paid $10 million in cash plus the value of the one-year repurchase option. *Ibid.* If the court of appeals had used $17,147,185 as the properties' value as petitioner urges, the value of the option that Tramiel gave also would have been much higher. That is because the option's value is calculated as the difference between the properties' value and the option's strike price. *Id.* at 12a-13a (citing *In re Calvillo*, 263 B.R. 214 (W.D. Tex. 2000)). If the value were $17,147,185, then because the strike price was calculated to be $10,432,815, the option would have been valued at $5,760,000. Thus, even under petitioner's theory, Tramiel already paid $10 million in cash plus an option valued at $5,760,000, for a total of $15,760,000. That makes his liability $1,387,185 ($17,147,185 minus $15,760,000), which is the exact same amount calculated by the court of appeals. *Id.* at 24a. And that liability is more than offset by the $4.5 million settlement credit. *Id.* at 33a. Accordingly, the end result would be the same even under petitioner's proposed rule: petitioner would recover nothing from Tramiel.

To be sure, when the district court (in its reversed decision) applied petitioner's proposed rule and used the full, undiscounted value of the properties, it failed to recalculate the value of the option to take the higher value into account. For the reasons explained above, that was erroneous. In any event,

this fact-bound inquiry does not warrant this Court's review. The important point is that even under petitioner's proposed rule, the court of appeals' judgment would be affirmed. Eugene Gressman et al., SUPREME COURT PRACTICE 248 (9th ed. 2007) (discussing *Sommerville v. United States*, 376 U.S. 909 (1964)).

III. THERE IS NO CONFLICT CONCERNING ENTITLEMENT TO SETTLEMENT CREDITS FOR CONSTRUCTIVE FRAUDULENT TRANSFER LIABILITY, AND THE DECISION BELOW IS CORRECT IN ANY EVENT

Petitioner argues that there is a conflict over whether entitlement to settlement credits for fraudulent transfer liability is governed by federal or state law. No such conflict exists. And even if it did, this case would be a poor vehicle to resolve it, because applying federal law would make no difference to the outcome of this case.

A. The Lower Courts Are Not In Conflict Over Whether Federal Or State Law Governs Entitlement To Settlement Credits When The Trustee Brings A Fraudulent Transfer Claim Under State Law

As to the question whether the $4.5 million settlement by the other defendants should offset Tramiel's liability, the court of appeals did not discuss the question presented here—whether state or federal law governs. But all three lower courts correctly applied California law, as Section 544 requires. The bankruptcy court explained that "when State law

forms the substance of the underlying claim, Federal Courts will apply State Court settlement procedures in determining whether a settlement credit is appropriate." Pet. App. 144a; *see also* Pet. App. 114a.

Petitioner identifies three court of appeals' decisions that he contends conflict with that application of state law. Pet. 27-28. None of them presents a clear conflict.

First, the Eleventh Circuit's opinion in *In re Prudential of Florida Leasing, Inc.*, 478 F.3d 1291 (11th Cir. 2007), did not discuss the precise issue here: whether state or federal law governs entitlement to settlement credits when a transfer is avoided under *state* law via Section 544(b). Indeed, language in the *Prudential* opinion suggests that if the court were to directly address that precise question, it might agree with the court of appeals' decision in this case. *Prudential* states that where "the Trustee file[s] a claim *under state law*" for fraudulent transfer, then "the right of [the transferee] to a reduction in the amount of its liability" on account of a settlement "would arise *under state law*." *Id.* at 1300 (emphasis added). But where "the Trustee has filed only *federal* claims against [the transferee]," *ibid.*, *federal* common law interpreting Section 550(d)—which provides that the "trustee is entitled to only a single satisfaction"—governs, *id.* at 1297 (emphasis added) (citation omitted).[2]

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[2] This illustrates one of many differences in pursuing claims pursuant to Section 544 versus pursuant to Section 548.

Nor is there conflict between the decision below and the Fourth Circuit's *unpublished* opinion in *Bowers v. Kuse Enterprises, Inc.* (*In re Florida Hotel Properties Limited Partnership Plan Trust Agreement*), 172 F.3d 43, 1998 WL 957455 (4th Cir. 1998) (table opinion). There, the Trustee had pursued a fraudulent transfer claim under *federal*, not *state*, law—specifically, Section 549. *Id.* at *1.

Likewise, the ruling below does not conflict with the Ninth Circuit's prior opinion in *In re Lendvest Mortgage*, 42 F.3d 1181 (9th Cir. 1994). *Lendvest* did not decide whether federal or state law applies, and it is not even clear which law the court applied. In any event, any intracircuit disagreement would not merit intervention by this Court.

Moreover, the court of appeals here did not explain why it applied state rather than federal law to determine whether Tramiel was entitled to a settlement credit. Pet. App. 25a-32a. If this issue is worthy of this Court's review, and if this Court is inclined to review it, it should await a decision in which the court of appeals sets forth its reasoning.

B. Even If There Were A Conflict, This Case Would Not Be A Suitable Vehicle To Resolve It

In any event, if the lower courts had applied petitioner's proposed rule here, the result would have been the same: Tramiel's liability would have still been satisfied by the settlement of the other defendants to avoid double recovery by the trustee.

Petitioner claims that there are two criteria for a settlement credit under federal law: (1) a finding of joint liability between the settling and non-settling defendants, and (2) an allocation of the settlement amount toward the claims on which the non-settling defendant is jointly liable. Pet. 29-30.

Here, the bankruptcy court found that Tramiel and the settling defendants were jointly liable for claims arising in connection with the fraudulent transfer. The bankruptcy court relied on the fact that the trustee alleged that both Tramiel and "also * * * the settling defendants were responsible for the estate's injuries arising out of the sale of the real property to Tramiel, and those claims were covered by the settlement at issue." Pet. App. 145a. The court found that there were some claims for which "the settling defendants and Tramiel were jointly liable" and that there were "other non-joint claims." *Ibid.* Petitioner claims that this was not sufficient for a finding of joint liability. Pet. 30 n.19. But the Ninth Circuit concluded otherwise. Pet. App. 32a. In any event, the factbound dispute over the sufficiency of this finding does not warrant this Court's review and is yet another reason why this case is not a suitable vehicle to review the question presented.

Additionally, the bankruptcy court stated that if it were to conduct an allocation of the settlement among the joint and non-joint claims, it would allocate sufficient settlement amounts to the fraudulent transfer claim such that Tramiel's liability would still be satisfied. The court stated: "I considered what I

might do in terms of allocating the settlement now. If I were to undertake an allocation at this point in the case, it's likely that I would follow the judgment that I've already entered, and I realized that result would really be the same as following the plain words of [Section 877 of the California Code of Civil Procedure]." *Id.* at 148a.

Accordingly, petitioner would not prevail even under the legal rule that he seeks to press in this Court. That is further reason to deny review. Gressman, *supra*, at 248.

CONCLUSION

For the foregoing reasons, the petition for a writ of certiorari should be denied.

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APPENDIX

CALIFORNIA CIVIL CODE

Division 4. General Provisions
Part 2. Special Relations of Debtor and Creditor
Title 2. Fraudulent Instruments and Transfers
Chapter 1. Uniform Fraudulent Transfer Act

§ 3439.04. Transfer with intent to defraud or transfer not given in exchange for value: Determining actual intent

(a) A transfer made or obligation incurred by a debtor is fraudulent as to a creditor, whether the creditor's claim arose before or after the transfer was made or the obligation was incurred, if the debtor made the transfer or incurred the obligation as follows:

(1) With actual intent to hinder, delay, or defraud any creditor of the debtor.

(2) Without receiving a reasonably equivalent value in exchange for the transfer or obligation, and the debtor either:

(A) Was engaged or was about to engage in a business or a transaction for which the remaining assets of the debtor were unreasonably small in relation to the business or transaction.

(B) Intended to incur, or believed or reasonably should have believed that he or she would incur, debts beyond his or her ability to pay as they became due.

(b) In determining actual intent under paragraph (1) of subdivision (a), consideration may be given, among other factors, to any or all of the following:

(1) Whether the transfer or obligation was to an insider.

(2) Whether the debtor retained possession or control of the property transferred after the transfer.

(3) Whether the transfer or obligation was disclosed or concealed.

(4) Whether before the transfer was made or obligation was incurred, the debtor had been sued or threatened with suit.

(5) Whether the transfer was of substantially all the debtor's assets.

(6) Whether the debtor absconded.

(7) Whether the debtor removed or concealed assets.

(8) Whether the value of the consideration received by the debtor was reasonably equivalent to the value of the asset transferred or the amount of the obligation incurred.

(9) Whether the debtor was insolvent or became insolvent shortly after the transfer was made or the obligation was incurred.

(10) Whether the transfer occurred shortly before or shortly after a substantial debt was incurred.

(11) Whether the debtor transferred the essential assets of the business to a lienholder who transferred the assets to an insider of the debtor.

(c) The amendment to this section made during the 2004 portion of the 2003-04 Regular Session of the Legislature, set forth in subdivision (b), does not constitute a change in, but is declaratory of, existing law, and is not intended to affect any judicial decisions that have interpreted this chapter.

CALIFORNIA CODE OF CIVIL PROCEDURE

Part 2. Of Civil Actions
Title 11. Contribution Among Joint Judgment Debtors
Chapter 1. Releases From and Contribution Among Joint Tortfeasors

§ 877. Effect of release, dismissal, or covenant not to sue or enforce judgment

Where a release, dismissal with or without prejudice, or a convenant not to sue or not to enforce judgment is given in good faith before verdict or judgment to one or more of a number of tortfeasors claimed to be liable for the same tort, or to one or more other co-obligors mutually subject to contribution rights, it shall have the following effect:

(a) It shall not discharge any other such party from liability unless its terms so provide, but it shall reduce the claims against the others in the amount stipulated by the release, the dismissal or the covenant,

or in the amount of the consideration paid for it whichever is the greater.

(b) It shall discharge the party to whom it is given from all liability for any contribution to any other parties.

(c) This section shall not apply to co-obligors who have expressly agreed in writing to an apportionment of liability for losses or claims among themselves.

(d) This section shall not apply to a release, dismissal with or without prejudice, or a covenant not to sue or not to enforce judgment given to a co-obligor on an alleged contract debt where the contract was made prior to January 1, 1988.

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v.

JACK TRAMIEL,
Respondent.

On Petition for Writ of Certiorari to the United States Court of Appeals for the Ninth Circuit

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INTRODUCTION

Petitioner filed his petition for a writ of certiorari with this Court on January 12, 2011. United States Supreme Court Rule 15.8 permits a party to call attention to new cases not available at the time of the party's last filing. Petitioner files this supplemental brief to call attention to *Ransom v. FIA Card Services, N.A.*, 131 S.Ct. 716 (2011), decided by this Court on January 11, 2011, and to its significance in this matter. *Ransom* is a new case that was not available when Petitioner filed his petition. It directly conflicts with the Decision on two separate points of law.

ARGUMENT

I. *Ransom* Requires Courts To Employ A Particular Method Of Statutory Construction. The Decision Fails To Employ That Method. Consequently, The Decision Directly Conflicts With *Ransom*.

In *Ransom*, this Court interpreted United States Code, Title 11 ("Code"), § 707(b)(2)(A)(ii)(1).[1] The method that this Court employed to interpret § 707(b)(2)(A)(ii)(1) also applies when interpreting other Code sections. The Decision fails, however, to employ that method when interpreting § 550. The failure leaves *Ransom* and the Decision in direct conflict.

Ransom involved a chapter 13 debtor who was seeking confirmation of his plan of reorganization.

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[1] All further references to "§" will be to sections of the Code.

Confirmation of the reorganization plan depended on whether "vehicle ownership costs" were "*applicable*" to the debtor despite his owning his vehicle free and clear.[2] *Ransom*, 131 S.Ct. at 723-24. The debtor argued that the vehicle ownership costs were applicable to him despite his not having such actual costs. *Id.* at 723, 726. The lower courts rejected his argument, and held that those costs were applicable to only those debtors who had actual vehicle ownership costs.

This Court affirmed the lower courts. It found that the term "*applicable*" had legal significance because its insertion into § 707(b)(2)(A)(ii)(I)[3] affected the section's meaning – *i.e.*, the term's insertion made vehicle ownership costs applicable to *only* those debtors with such actual costs, while its omission would make the costs applicable to *all* vehicle-owning debtors. *Id.* at 724, 727. More particularly, the Court stated:

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[2] § 707(b)(2)(A)(ii)(I) includes "vehicle ownership costs" among a debtor's *applicable* "monthly expenses." Under § 1325, these monthly expenses may be used to calculate a debtor's "disposable income," all of which must be paid through the debtor's plan of reorganization before the plan can be confirmed over objections.

[3] In relevant part, § 707(b)(2)(A)(ii)(I) states:

> The debtor's monthly expenses shall be the debtor's *applicable* monthly expense amounts specified under the National Standards and Local Standards, and the debtor's actual monthly expenses for the categories specified as Other Necessary Expenses issued by the [IRS] for the area in which the debtor resides.

(emphasis added).

> If Congress had not wanted to separate in this way debtors who qualify for an allowance from those who do not, it could have omitted the term "*applicable*" altogether. Without that word, all debtors would be eligible to claim a deduction for each category listed in the Standards. Congress presumably included "*applicable*" to achieve a different result. [citation omitted] Interpreting the statute to require a threshold determination of eligibility ensures that the term "*applicable*" carries meaning, as each word in a statute should.
>
> ***
>
> [Debtor's] interpretation would render the term "*applicable*" superfluous . . . . The word "*applicable*" is not necessary to [achieve Debtor's interpretation]; it is necessary only for the different purpose of dividing debtors eligible to make use of the tables from those who are not.

Id. at 724, 727 (emphasis added). Due to this Court's recognizing that "*applicable*" has legal significance, it refused to render the term superfluous, and found that § 707(b)(2)(A)(ii)(1) means that vehicle ownership costs are applicable to *only* those debtors with actual vehicle ownership costs. *Id.* at 724-26, 730.

The dissent in *Ransom* agreed with the majority that the fairest reading of § 707(b)(2)(A)(ii)(1) depended on the interpretation of "*applicable*." *Id.* at 731-32 & n.* (Scalia, J. dissenting). It disagreed, however, with the majority's ascribing a definition of legal significance to the term. Instead, it stated that

Congress never intended the term to have legal significance because, according to the dissent, § 707(b)(2)(A)(ii)(1)'s has the same meaning with or without the inclusion of "*applicable*." *Id*. Because it believed that the meaning of § 707(b)(2)(A)(ii)(1) was unchanged by the inclusion of "*applicable*," the dissent rejected the majority's view of the key issue - *i.e.*, whether to render a legally significant term superfluous. Instead, it viewed the issue as whether to interpret an intentionally meaningless term in a manner that recognized and respected Congressional verbosity. *Id*. at 731. Thus, the dissent believed that § 707(b)(2)(A)(ii)(1) made vehicle ownership costs applicable to all vehicle-owning debtors.

Ransom, of course, would have little effect here if the Decision had accepted the contention in Petitioner's petition that § 550(b)-(f)'s defenses are rendered exclusive by the plain meaning of § 550's limiting phrase – "*except as otherwise provided in this section*."[4] Instead, *Ransom* acquires acute relevance to this matter because the Decision did not recognize and apply § 550's plain meaning.

If the plain meaning of the limiting phrase is ignored, *Ransom* would require that the phrase be subjected to the same analysis to which "*applicable*" was subjected. In other words, it would be necessary to determine whether inserting "*except as otherwise provided in this section*" into § 550 affected the

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[4] *See e.g., Crosby v. U.S.*, 506 U.S. 255, 258-59 (1993) (holding that "it could not be more clear" that "*except as otherwise provided in this rule*" is a limiting phrase that renders exclusive those provisions to which it refers in Criminal Rules of Federal Procedure 43).

section's meaning. And if so, both the majority and the dissent in *Ransom* would require the adoption of a meaning for § 550 that treated the limiting phrase as having legal significance.

Inserting "*except as otherwise provided in this section*" into § 550 did, in fact, affect § 550's meaning. It made § 550(b)-(f)'s defenses exclusive, while its omission would have made § 550(b)-(f)'s defenses non-exclusive. Thus, *Ransom* would require courts to respect the limiting phrase's legal significance, and interpret § 550 to mean that § 550(b)-(f)'s defenses are exclusive. The Decision's finding that § 550(b)-(f)'s defenses non-exclusive, therefore, directly conflicts with *Ransom*.

II. *Ransom* Requires Courts To Define A Statutory Term According To Its Ordinary Meaning. The Decision Fails To Define "Value" According To Its Ordinary Meaning. Consequently, The Decision Directly Conflicts With *Ransom*.

The *Ransom* Court found that an undefined Code term should be construed according to its ordinary meaning. *Ransom*, 131 S.Ct. at 724. Thus, it interpreted "*applicable*" in § 707(b)(2)(A)(ii)(1) to mean "appropriate, relevant, suitable, or fit." *Id*.

Unlike Ransom, however, the Decision fails to interpret "value" according to its ordinary meaning. As stated in the petition, the ordinary meaning of "value" outside of the foreclosure context is "fair

market value."[5] But instead of assigning "value" its ordinary meaning, the Decision defines "value" to mean "reasonably equivalent value." "Reasonably equivalent value" is a "neologism"[6] And by definition, a neologism cannot constitute an ordinary meaning. In fact, "reasonably equivalent value" is not an actual value. It is a term used to evoke a judicial inquiry into whether there is a relationship of approximate equivalence between a property's actual value and the value that the transferor received for the property.[7] The Decision, therefore, directly conflicts with Ransom by foregoing the ordinary meaning of "value" in favor of a novel meaning that represents a relationship between two separate values rather than an actual value.

CONCLUSION

Denying certiorari regarding a decision that directly conflicts with this Court's prior holding necessarily sows confusion among the various courts of appeals. Such denial raises questions about whether this Court is considering a retreat from its prior holding, or whether it is calling for a change in how the holding must be applied.

Here, because the Decision directly conflicts with *Ransom*, denying the petition for certiorari will cause the lower courts to become uncertain about how or if to consider the *Ransom* factors when determining

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[5] *BFP v. Resolution Trust Corp.*, 511 U.S. 531, 537-39 (1994).

[6] *Id.* at 537.

[7] *Id.* at 537-39 & n.4, 546

whether they are rendering a legally significant term superfluous. Similarly, the courts of appeals will be left to wonder whether this Court will no longer abide by its past definition of "value" in bankruptcy matters or by its past pronouncements that a statutory term should be defined according to its ordinary meaning. For these reasons, the direct conflict between *Ransom* and the Decision requires that this Court grant the petition for certiorari.

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Alan N. Resnick & Henry J. Sommer, 5 *Collier on Bankruptcy*, § 548.01B (16th ed. 2010) 3

I. STATE AVOIDANCE LAW IS SEPARATE AND DISTINCT FROM FEDERAL RECOVERY LAW.

Petitioner[1] asks this Court to grant certiorari to resolve several outcome-determinative conflicts existing between the Decision and cases decided by both this Court and various courts of appeals. The conflicts involve *federal* law because they arise under the §550 *recovery* statute.

Respondent asserts there are no conflicts involving federal law. He maintains that the Decision turns on the application of *state avoidance* law as applied via §544(b). (Thus, Respondent tacitly admits that certiorari would be proper if the conflicts involve federal recovery law under §550.)

Respondent's belief that federal law is not at issue is mistaken. Respondent believes that the Decision uses UFTA §8(d) as a defense to *avoidance* of the Transfer under state law (as made applicable by §544(b)) rather than as a defense to the amount of *recovery* under the federal bankruptcy law, §550. Opp. 1, 16-17. He is wrong. The Code considers avoidance and recovery to be distinct concepts controlled by separate sections. *In re Burns*, 322 F.3d 421, 427 (6th Cir. 2003). And UFTA §8(d) is a recovery statute, not an avoidance statute. *See e.g., Freeman v. First Union Nat.*, 329 F.3d 1231, 1233-34 (11th Cir. 2003) (distinguishing §550 and UFTA §7 [to which UFTA §8 is a defense] from §548 and UFTA §4).

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[1] Petitioner incorporates the defined terms used in his petition.

The Decision clearly treats UFTA §8(d) as a recovery statute by applying it as a defense to §550 and not to §544(b). It expressly states that the Transfer is fraudulent and *void* under *UFTA §4(a)*. It invokes *UFTA §8(d)* only as a defense to reduce *recovery* under §550. It states:

> The *Acequia* test requires that the trustee show *(1) fraud* or illegality; *(2) voidness* of the transfer under §544(b) and applicable law; and *(3) liability* of the particular transferee under §550. [citation omitted.] In this case, the trustee has satisfied *steps one and two* by showing that the real property transfer from JTS to Tramiel was a constructive fraudulent conveyance and *was void* under §544(b) and California Civil Code *§3439.04(a)*. The trustee has also shown that Tramiel has liability for the transfer, but the amount of *recovery* must be calculated to the extent that it benefits the estate, as *§550* expressly requires....
>
> To calculate the amount of *recovery* and abide by the intent of *§550*, we hold that California Civil Code §*3439.08(d)*, the good faith transferee exception, applies in §544(b) cases and, if satisfied, allows for a reduction in the trustee's *recovery*....

App. 23a (emphasis added).

Because the Decision applied UFTA §8(d) as a defense to §550, the resulting conflicts involve federal recovery law. Therefore, certiorari is appropriate on that issue.

The remainder of Respondent's opposition to certiorari also flows from his mistaken view of UFTA §8(d) and whether it results in partial avoidance. He argues that "value" in §550 should equal a property's reasonably equivalent value because the Transfer is partially avoided under UFTA §8(d) to the extent of the Parcels' reasonably equivalent value. And he posits that because the Transfer was only partially void under state law, state procedure should control whether he is entitled to a settlement credit. As explained below, Respondent's positions simply are not grounded in the language of the Decision or in the plain meaning of the relevant statutes.

Last, Respondent attempts to distinguish and discredit Petitioner's authorities. The remainder of this Reply addresses these attempts

II. THE DECISION ACTUALLY CONFLICTS WITH THE SEVENTH CIRCUIT REGARDING WHETHER INITIAL TRANSFEREES MAY ASSERT UFTA §8 DEFENSES.

The Seventh Circuit does not allow initial transferees to assert UFTA §8(d) in §550 actions.[2] *In re Boyer*, 2009 WL 418275, at 16* (N.D. Ind. Feb. 17, 2009), *aff'd Boyer v. Crown Stock Distribution, Inc.*, 587 F.3d 787, 798 (7th Cir. 2009). In stark contrast, the Ninth and Eleventh Circuits allow initial transferees to assert that defense. App. 23a, 25a; *In re Kingsley*,

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[2] Forty-three states and the District of Columbia have adopted UFTA. Alan N. Resnick & Henry J. Sommer, 5 *Collier on Bankruptcy*, § 548.01B (16th ed. 2010).

2007 WL 1491188, at *4-6 (Bankr. S.D.Fla. May 17, 2007), *aff'd* 518 F.3d 874, 877-78 (11th Cir. 2008).

Respondent argues that the Decision is not in actual conflict with *Boyer* because the Seventh Circuit does not discuss *Boyer's* good-faith shareholder transferees' UFTA §8(d) defense. Respondent provides no authority for his position. Appellate courts of appeals need only to consider and necessarily decide an issue to create conflicts worthy of certiorari. *See Anderson v. Celebrezze,* 460 U.S. 780, 784 n.5, 786 & n.6 (1983).

Respondent only disputes whether the Seventh Circuit necessarily decided the issue.[3] He alleges that UFTA §8(d) was rendered moot by the good-faith shareholder transferees' failure to provide value to the debtor. The defense was not moot, and the Seventh Circuit necessarily decided it.

Respondent urges that UFTA §8(d) was moot in *Boyer* because the good-faith shareholder transferees never provided any value. But UFTA §8(d) requires only that transferees act in good faith and that *debtors receive* value; it does not require that good-faith *transferees provide* any value. *Compare* UFTA §8(d) (debtor receiving value) *with* UFTA §8(a) (transferee providing value). Because *Boyer's* good-faith shareholder transferees qualified for a UFTA §8(d) defense by virtue of having acted in good faith and the debtor's having received value, they would have been

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[3] There is no dispute that the Seventh Circuit had the issue before it. *See* Appellee/Cross-Appellant's Brief, 2009 WL 1900130, Argument VII, pages 36-41.

entitled to assert the defense unless it was precluded by §550. And when the lower courts discussed whether UFTA §8(d) was applicable, they considered only whether §550 allowed for it. *Boyer*, 2009 WL 418275 at *15; *In re Crown Unlimited Machine, Inc.*, 2006 WL 6401548 at *12 (Bankr. N.D. Ind. Oct. 13, 2006). They did not discuss whether the good-faith shareholder transferees gave value. Thus, the courts' refusal to allow the defense was necessarily based solely on UFTA §8(d)'s being unavailable under §550.

The lower courts' only discussion regarding whether *Boyer's* good-faith shareholder transferees gave value took place in the narrow context of deciding whether the transferees were eligible for a §550(b) defense. *Boyer*, 2009 WL 418275 at *14-15; *Crown Unlimited Machine,* 2006 WL 6401548 at *14-15. Similarly, the Seventh Circuit's discussion regarding whether *Boyer's* good-faith shareholder transferees gave value also came within only that narrow context. *Boyer*, 587 F.3d at 796. The Seventh Circuit left the lower courts' reasoning and findings undisturbed regarding their refusal to allow UFTA §8(d). Otherwise, the Seventh Circuit would had to have granted the UFTA §8(d) defense to the good-faith shareholder transferees because the debtor received value.

Based on the above, Respondent's argument serves as no barrier to finding that *Boyer* constitutes an actual conflict with the Decision (and *Kingsley*) that is worthy of certiorari under *Anderson*.

III. THE DECISION ACTUALLY CONFLICTS WITH VARIOUS COURTS OF APPEALS REGARDING WHETHER INITIAL TRANSFEREES ARE STRICTLY LIABLE IN §550 ACTIONS.

The Second, Sixth, and Tenth Circuit Courts of Appeals hold that initial transferees are *strictly liable* under §550. *See e.g., In re Red Dot Scenic, Inc.*, 351 F.3d 57, 58 (2nd Cir. 2003); *In re Hurtado*, 342 F.3d 528, 532-33, 534 n.2 (6th Cir. 2003); *Rupp v. Markgraf*, 95 F.3d 936, 944 (10th Cir. 1996). Nonetheless, the Decision finds Respondent has no liability despite being an initial transferee.

Respondent argues that the other courts of appeals' cases are not in actual conflict with the Decision because they are distinguishable. He asserts that, unlike the other cases, the Decision involves "whether the transaction itself is *avoidable* and, if so, in what amount." Opp. 18 (emphasis added).

Respondent's distinction is faulty. As discussed above, he erroneously assumes that UFTA §8(d) is a defense against avoidance rather than against recovery. Thus, the above cases are not distinguishable.

IV. THE DECISION ACTUALLY CONFLICTS WITH THIS COURT REGARDING §550'S PLAIN MEANING AND THE NECESSITY OF APPLYING THAT PLAIN MEANING.

§550 contains the common limiting phrase "[e]xcept as otherwise provided in this section." §550's limiting phrase refers to the defenses expressly provided in

§550(b)-(f). This Court has established that the limiting phrase's plain meaning renders *exclusive* those provisions to which it refers. *Crosby v. U.S.*, 506 U.S. 255, 258-59 (1993)(Fed.R.Crim.P. 43), *see also U.S. v. Gbemisola*, 225 F.3d 753, 758 (D.C. Cir. 2000)(contrasting 18 U.S.C. §3117 with 18 U.S.C. §§2511(a), 3121(a)). Any other interpretation of the limiting phrase would affect the exclusivity of the other 11,025 federal code sections, rules, and regulations in which it appears.[4] Thus, as a matter of the limiting phrase's plain meaning, §550's expressly provided defenses are exclusive of all other defenses, including UFTA §8(d).

This Court also holds that a statute's plain meaning must be applied regardless of the statute's history or underlying policy. *Lamie v. U.S. Trustee*, 540 U.S. 526, 534 (2004). Consequently, the Decision actually conflicts with *Crosby* and *Lamie* because, rather than holding that §550's defenses are exclusive and barring UFTA §8(d), it applies UFTA §8(d) as a defense to §550 recovery.

In addition to failing to consider *Crosby* or *Lamie*, Respondent misapplied §550 by *literally* eliminating the limiting phrase that controls its defenses' exclusivity.[5] Instead, he focuses on the phrase "to the

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[4] Computed via Westlaw.

[5] In relevant party, §550 reads as follows:

> *Except as otherwise provided in this section*, to the extent that a transfer is avoided under section 544 ...

(emphasis added)

extent," which immediately follows the limiting phrase. He argues that, because the Transfer is only partially void under §544(b), §550 allows a recovery of the value of the Properties "to the extent" of the partial avoidance. Opp. 21-22. As discussed above, Respondent mistakenly presumes that the Decision found the Transfer was only partially avoided.

Respondent also disputes whether the Decision actually conflicts with *In re Straightline Investments, Inc.*, 525 F.3d 870 (9th Cir. 2008). He attempts to distinguish *Straightline* because its avoidance took place under §549(a) rather than under §544(b). But that factual distinction is immaterial. As here, *Straightline's* transfer was fully avoided, and the transferees' attempt to assert a state law defense involved §550, not the Code's avoidance sections.

Additionally, Respondent contends that the Decision and *Straightline* do not actually conflict because he acted in good-faith and the *Straightline* transferee engaged in inequitable conduct. Respondent's contention is false. *Straightline* specifically noted that §550's preclusion of state law

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As in the Decision, App. 15a, Respondent's reference to §550 omits the limiting phrase and quotes only the text immediately following it. He states:

> Section 550(a) provides that the trustee may recover from initial transferees either the property transferred or the value of such property, but only *"to the extent that a transfer is avoided under section 544."*

Opp. 21 (emphasis added).

defenses applied equally to good-faith transferees. It stated:

> *Even a good faith transferee* is not protected beyond a possible lien on the property, and he is only protected if he is the initial transferee. *Id.* §550(a)-(b), (e). Section 550 is thus substantially less protective of transferees than it is of the estate.

Straightline, 525 F.3d at 884-85 (emphasis added).

Respondent alleges that even if the Decision and *Straightline* actually conflict, certiorari still would be inappropriate because it would be an intracircuit conflict. *Maggio v. Zeitz*, 333 U.S. 56, 59-60 (1948), and *John Hancock Mut. Life Ins. Co. v. Bartels*, 308 U.S. 180, 181 & n.1 (1939), however, demonstrate that intracircuit conflicts are sufficient to grant certiorari in bankruptcy matters.

Finally, Respondent denies that the Decision partially relied on its novel belief that "recoveries available under state law through Section 544(b) must be the same as those available under federal law in Section 548." Opp. 23. But the Decision clearly requires symmetry between §548(c) and §544(b). App. 23. It states:

> Moreover, allowing state law good faith transferee exceptions in cases asserting §544 claims permits a symmetry with the Bankruptcy Code: §548 of the Bankruptcy Code, which voids fraudulent transfers under federal law, allows for a reduction in recovery due to a

> good faith transferee. *Section 544(b) ... should reflect this symmetry.*

App. 25a (emphasis added).

V. THE DECISION ACTUALLY CONFLICTS WITH THIS COURT AND VARIOUS COURTS OF APPEALS REGARDING THE MEANING OF "VALUE."

This Court found that the ordinary meaning of "value" is *fair market value*. *BFP v. Resolution Trust Corp.*, 511 U.S. 531, 537-38, 547-48 (1994). A fundamental canon of statutory construction is that statutory terms are given their ordinary meaning. *Perrin v. United States*, 444 U.S. 37, 42 (1979). Thus, this Court assigned to "value" its ordinary meaning to describe the worth of property that is not subject to foreclosure. *BFP*, 511 U.S. at 537-38, 547-48 (construing §548); *American Commercial Corp. v. Rash*, 520 U.S. 953, 960-65 (1994)(construing §506(a)). The ordinary meaning of "value" should carry over into §550 because Code provisions used in different sections should share the same meaning. *Sullivan v. Stroop*, 496 U.S. 478, 484 (1990). The above precedents actually conflict with the Decision, which defines "value" in §550 as a property's *reasonably equivalent value*.

Respondent attempts to distinguish *BFP* and *Rash*, arguing they define "value" only for purposes of federal law. But §550 is federal law. Thus, *BFP* and *Rash* are controlling precisely because they define "value" for purposes of federal law.

In fact, reasonably equivalent value cannot determine liability under §550 because it represents a relationship, not an actual value. Reasonably equivalent value represents only a comparative relationship between two other values – *i.e.*, a transferred property's actual value and the value of the consideration paid for it. *See In re Fruehauf Trailer Corp.*, 444 F.3d 203, 212–13 (3rd Cir. 2006); *In re Fordu*, 201 F.3d 693, 707 (6th Cir. 1999); *Barber v. Golden Seed Co., Inc.*, 129 F.3d 382, 387 (7th Cir. 1997); *In re Morris Communications NC, Inc.*, 914 F.2d 458, 466–67 (4th Cir. 1990).

Finally, Respondent asserts that to interpret "value" under §550 to mean fair market value would not impact his liability, which is zero under the Decision. This assertion is overly presumptuous and mathematically incorrect. It is based on three presumptions: 1) §550 allows him to assert a state law defense reducing his liability by the $10,432,815 he paid; 2) he is entitled to a $4,500,000 settlement credit based on state procedure (discussed below); and 3) the first two presumptions will completely eliminate his liability for the Properties' $17,147,185 fair market value. The first two presumptions are unsupported by the law. The third is wrong as a matter of arithmetic.

VI. THE DECISION ACTUALLY CONFLICTS WITH THIS COURT AND VARIOUS COURTS OF APPEALS REGARDING WHETHER FEDERAL PROCEDURE SHOULD DETERMINE THE AWARD OF SETTLEMENT CREDITS IN §550 RECOVERY ACTIONS.

Federal procedure controls actions involving claims arising under federal schemes that require uniformity. *Kamen v. Kemper Financial Services, Inc.*, 500 U.S. 90, 98 (1991); *U.S. v. Kimbell Foods, Inc.*, 440 U.S. 715, 728-29 (1979). Under federal procedure, the two criteria for allowing settlement credits are: (1) a finding that the settling and non-settling defendants are jointly liable; and (2) an allocation of relative culpability. *McDermott, Inc. v. AmClyde*, 511 U.S. 202, 216-17, 218-21 (1994).

Bankruptcy is a federal scheme that requires uniformity. U.S. Constitution, Article I, Section 8, Clause 4. Thus, §550 recovery actions are subject to federal procedure, *In re Prudential of Florida Leasing Inc.*, 478 F.3d 1291, 1298-99, 1301-02 (11th Cir. 2007), and *McDermott's* federal criteria are applied to determine whether settlement credits are appropriate in §550 actions. *Bowers v. Kuse Enters., Inc.*, 1998 WL 957455, at *7 (4th Cir. Sept. 22, 1998); *In re Lendvest*, 42 F.3d 1181, 1184 (9th Cir. 1994).

Respondent argues that *Prudential of Florida*, *Bowers*, and *Lendvest* are distinguishable because they discuss only whether federal procedure is applicable to §550, not whether it is applicable to the underlying state avoidance statutes. But it is the §550 recovery liability that will affected by any settlement credit, not

avoidance. Thus, it is the federal nature of §550 that controls which procedure applies.

In the alternative, Respondent argues that if federal procedure does control, the federal criteria for him to receive a settlement credit are met. Untrue.

Respondent alleges that the bankruptcy court found joint liability. But that court found only that Petitioner's complaint alleged joint liability, which is singularly sufficient to grant a settlement credit under *state law*. Pet. 7 n.6, 11 n.7. It did not find actual joint liability, which is what *federal procedure* requires for awarding settlement credits.[6] Pet. 30 n.19.

Respondent's assertion that the bankruptcy court allocated culpability is equally flawed. He relies on the bankruptcy court's oral comment that any allocation the court *would have* made would have satisfied California's allocation requirement. App. 148a. Unlike federal law, California law only requires an allocation of *liability*, which is not required to equal the parties' share of *culpability*. *Rutgard v. Haynes*, 61 F.Supp.2d 1082, 1086 (S.D.Cal. 1999)(culpability does not necessarily equal an allocation of liability in a settlement credit because culpability is only one factor used to determine the allocation of liability), *citing Tech-Bilt, Inc. v. Woodward-Clyde & Assoc.*, 38 Cal. 3d 488, 499 (1985). In fact, "culpability" and "liability" represent different concepts and their

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[6] Respondent alleges that the Decision's determination that the bankruptcy court found joint liability is a matter of fact. Respondent provides no authority stating that such a determination is one of fact rather than of procedural review.

allocations serve different functions. "Culpability" connotes blameworthiness. *Black's Law Dictionary*, at 385 (7th ed. 1999). Its allocation promotes fairness between jointly liable co-defendants. *Baird v. Jones*, 21 Cal. App. 4th 684, 689-93 (1993). "Liability," however, means a legal obligation. *Black's*, at 925. And its allocation functions to prevent plaintiffs from receiving double recoveries for the same injury. *McComber v. Wells*, 72 Cal. App. 4th 512, 517 (1999). Consequently, the bankruptcy court's statement was not an allocation of culpability.

CONCLUSION

For the above reasons, not only should the petition for certiorari be granted, but grounds exist for a summary reversal. *Felkner v. Jackson*, 131 S.Ct. 1305 (2011).

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Respectfully submitted,

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